

Commercial Bank of Qatar (CBQK)

Recommendation	OUTPERFORM	Risk Rating	R-3
Share Price	QR7.311	Target Price	QR8.904
Implied Upside	21.8%	Old Target Price	QR7.995

Attractive Valuation Relative to Growth; Hiking PT & Upgrading to Outperform

We forecast 2021-26e earnings CAGR of 17.6% (vs. 15.8% previously) and this double-digit growth is due to strong core banking income, cost containment and a drop in CoR (major determinant). Hence, our new sustainable RoE rises to 16.2% vs. 15.4% previously. The stock remains attractive with undemanding multiples. CBQK is trading at a 2022/23 P/TB of 1.5x/1.4x based on our estimates. The stock is also trading at a PEG of 0.7x (which is inexpensive) based on our 5-year earnings CAGR of 17.6% (2021-26e). Moreover, the market is pricing in a sustainable RoE of 15.0%, which is lower than our forecast. We increase our PT to QR8.904 and upgrade our rating from Accumulate to Outperform.

Highlights

- 1H2022 bottom-line was driven by strong core banking income and cost containment; however, hyperinflation accounting shaved off 4.6% from the bottom-line. Commercial Bank of Qatar (CBQK) reported a net profit of QR1.43bn in 1H2022, growing by 7.9% YoY. Earnings before hyperinflation accounting was up by 13.1%.
- Goodwill impairments on UAB (40.0% stake) should come to end in 4Q2022. Management will book further impairments on UAB in 4Q2022. CBQK carried goodwill attributed to UAB of QR1.4bn in 2018. In 2019 & 2020, CBQK impaired QR413.9mn and QR591.2mn, respectively. Moreover, it impaired QR291.0mn in 2021. Hence, ~QR100mn of goodwill remains. We model remaining impairments of ~QR100mn in 4Q2022, ending this exercise.
- RoE is estimated to increase from 11.0% in 2021 to 12.7% in 2022e (we were modeling 13.3% previously for 2022). After 2022, we model RoE to increase beyond 14%. Management is targeting 13-15% during 2022-26 (although we believe RoE could slightly increase above the upper end of guidance). Our new sustainable RoE is 16.2% vs. 15.4% previously.
- Majority of NPLs are real estate legacy loans; management is guiding for the NPL ratio to decrease to 2.5% by 2026. NPL ratio decreased from 4.66% in FY2021 to 4.55% in 1H2022. Coverage of Stage 3 loans improved from 62% in FY2021 to 66% in 1H2022. Stage 2 loans improved from 15.9% in FY2021 to 15.2% in 1H2022. Going forward, we expect asset quality to improve, driven by conservative underwriting and recoveries. Management will also raise the coverage of Stage 3 loans to 100%.
- CoR in 2022 is expected at 100-110bps as per management's guidance and should normalize in the range of 60-80bps by 2026. 1H2022 provisions for credit losses increased by 20.8% YoY to QR501.8mn, while CoR (annualized) increased from 80bps in 1H2021 to 95bps. Moreover, management is being prudent/conservative by booking large provisions. We model in a CoR of 105bps for 2022 and 95bps in 2023. We estimate CoR to decline to 71bps by 2025 and 64bps (2026), in-line with management's guidance.
- Diversification of loan book remains on track; management is guiding for 25/16% public sector/real estate mix. During 2Q2022, net loans sequentially moved up by 2.9% (+3.3% vs. FY2021) to QR101.2bn. Moreover, deposits expanded by 5.7% QoQ and 9.0% vs. FY2021 to QR89.3bn. Moreover, in-line with management's strategy, % of govt. loans to total loans increased from 2016's 10% to 16% in 1H2022 (decreased from 2021's 18% due to govt. repayments), while real estate loans dropped from 28% to 20% during the same period. We estimate net loan growth of 4.6% in 2022 vs. 6.8% previously. Our loan growth assumptions have not changed; we pencil in a 2021-26e CAGR of 6.2% vs. 4.7% (2016-21).
- CET1 ratio is expected at 13.0%-14.0% (2022-26) as per management's guidance. Based on our estimates, we expect the bank to generate a CET1 ratio of 11.6% in 2022 and steadily reach 13.0% by 2026.

Catalysts

- Significant RoE expansion & robust bottom-line growth

Recommendation, Valuation and Risks

- Recommendation and valuation:** We raise our PT to QR8.904 and upgrade the stock to an **Outperform**. CBQK is trading at a 2023e P/TB and P/E of 1.4x and 10.1x, respectively.
- Risks:** 1) Weakness in Turkish Lira & Hyperinflation & 2) Goodwill impairments in NBO 3) Higher than expected CoR

Key Financial Data and Estimates

(In QR mn)	2021	2022e	2023e	2024e
EPS	0.490	0.572	0.723	0.859
EPS Growth (%)	89.6	16.8	26.4	18.8
P/E (x)	14.9	12.8	10.1	8.5
Tangible BVPS (QR)	4.5	4.8	5.3	6.0
P/TBV (x)	1.6	1.5	1.4	1.2
RoE (%)	11.0	12.7	15.0	16.1
DPS (QR)	0.160	0.200	0.250	0.300
Dividend Yield (%)	2.2	2.7	3.4	4.1

Source: Company data, QNB FS Research; Note: All data based on current number of shares

Key Data

Current Market Price (QR)	7.311
Dividend Yield (%)	2.2
Bloomberg Ticker	CBQK QD
ADR/GDR Ticker	-
Reuters Ticker	COMB.QA
ISIN	QA0007227752
Sector*	Banks & Fin Svcs.
52wk High/52wk Low (QR)	8.689/5.918
3-m Average Volume (mn)	6.24
Mkt. Cap. (\$ bn/QR bn)	8.1/29.6
Shares Outstanding (mn)	4,047.25
FO Limit* (%)	100.0
Current FO* (%)	24.9
1-Year Total Return (%)	25.5
Fiscal Year End	December 31

Source: Bloomberg (as of September 15, 2022), *Qatar Exchange (as of September 15, 2022); Note: FO is foreign ownership

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Valuation

We value CBQK using the Residual Income Model (RI) based on a fundamental P/B:

We derive CBQK's fair value by employing the RI valuation technique (*based on a fundamental P/B*), which is calculated based on the sum of its beginning book value, present value of interim residuals (net income minus equity charge) and the present value of the terminal value (we apply a fundamental P/B multiple based on the Gordon Growth Model to the ending book value at the end of our forecast horizon). We derive the P/B from the Gordon Growth Model: $P/B = (RoE-g)/(Ke-g)$. This model uses sustainable return on equity (RoE) based on the median over our forecast period, cost of equity (Ke) and expected long-term growth in earnings (g) to arrive at fundamental/justified P/B. **Based on this method, we arrive at a fundamental P/B of 1.7x.**

We add Qatar's 10-year CDS rate of 0.76% to the 10-year US government bond yield (3.2%) to arrive at a risk free rate of 4.0%. We factor in an adjusted beta of 0.92x. Finally, we add an equity risk premium of 8.30% to arrive at a Ke of 11.59%.

Valuation Methodology

Fundamental P/B		RI Based on Fundamental P/B	
Sustainable RoE (%)	16.18	Beginning BVPS (2021) (QR)	4.510
Estimated Cost of Equity (%)	11.59	Present Value of Interim Residuals (QR)	1.249
Terminal Growth Rate (%)	5.0	Present Value of Terminal Value (QR)	3.164
Fundamental P/B	1.7x	Less: Intangibles & Goodwill	0.019
		Fundamental P/B	1.7x
		Intrinsic Value (QR)	8.904
		Current Market Price (QR)	7.311
		Upside/(Downside) Potential (%)	+21.8%

Source: QNB FS Research

Forecasts

	2022e	2023e	2024e	2025e	2026e	2027e	2028e	Terminal
Beginning BVPS	4.51	4.85	5.37	5.98	6.66	7.46	8.33	9.20
Attributable EPS	0.57	0.72	0.86	0.98	1.10	1.21	1.28	1.34
DPS	0.16	0.20	0.25	0.30	0.30	0.35	0.40	0.40
Adjustment	-0.08	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Ending BVPS	4.85	5.37	5.98	6.66	7.46	8.33	9.20	10.14
Equity Charge	0.52	0.56	0.62	0.69	0.77	0.87	0.97	1.07
Residual Income	0.05	0.16	0.24	0.29	0.33	0.35	0.31	0.27
Terminal Value (Based on Fundamental P/B)								7.1
Discounted Interim Residuals	0.05	0.14	0.18	0.20	0.21	0.19	0.15	0.12
Discounted Terminal Value								3.16

Source: QNB FS Research

Detailed Financial Statements

Income Statement (In QR mn)	2019	2020	2021	2022e	2023e	2024e
Net Interest Income	2,963	3,100	3,702	4,076	4,469	4,900
Fees & Commissions	915	811	928	911	958	1,008
FX Income	281	296	309	316	290	282
Other Income	181	(180)	291	284	347	362
Non-Interest Income	1,377	927	1,528	1,511	1,595	1,652
Total Revenue	4,340	4,027	5,230	5,587	6,064	6,553
Operating Expenses	(1,228)	(1,096)	(1,480)	(1,396)	(1,459)	(1,540)
Net Operating Income	3,112	2,931	3,750	4,192	4,605	5,013
Net Provisions & Impairments	(1,068)	(1,615)	(1,438)	(1,372)	(1,213)	(1,091)
Net Profit Before Taxes	2,044	1,316	2,313	2,820	3,392	3,922
Tax	(23)	(15)	(9)	(34)	(41)	(47)
Net Profit Before Minority Interest	2,021	1,301	2,304	2,786	3,352	3,875
Minority Interest	(0)	(0)	(0)	(0)	(0)	(0)
Non-Recurring Income/(Loss)				(140)	(80)	(40)
Net Profit (Headline/Reported)	2,021	1,301	2,304	2,646	3,272	3,835
Interest on Tier-1 Note	(240)	(223)	(264)	(264)	(264)	(264)
Social & Sports Contribution Fund	(50)	(33)	(58)	(66)	(82)	(96)
Net Profit (Attributable)	1,731	1,046	1,983	2,316	2,926	3,475

Source: Company data, QNB FS Research

Balance Sheet (In QR mn)	2019	2020	2021	2022e	2023e	2024e
Cash & Balances with Central Bank	6,075	8,279	17,915	13,683	13,782	14,985
Interbank Loans	12,396	10,401	10,942	17,507	17,682	14,146
Net Investments	26,844	25,778	26,723	29,122	31,670	33,599
Net Loans	88,009	96,698	98,003	102,553	108,001	115,449
Investment In Associates	4,021	3,117	2,961	2,984	3,111	3,242
Other Assets	2,569	3,005	2,567	3,077	3,240	3,002
Net PP&E	2,854	3,158	2,753	2,619	2,833	2,836
OREO	4,531	2,995	3,524	3,524	3,524	3,524
Goodwill & Intangible Assets	236	175	75	75	75	75
Total Assets	147,536	153,606	165,464	175,144	183,918	190,857
Liabilities						
Interbank Deposits	22,531	20,007	17,777	20,849	23,481	20,091
Customer Deposits	76,297	75,790	81,958	91,220	95,051	99,899
Term Loans	21,568	27,233	31,005	28,524	30,236	32,866
Tier-1 Perpetual Notes	4,000	4,000	5,820	5,820	5,820	5,820
Other Liabilities	5,385	8,406	10,651	9,122	7,604	7,992
Total Liabilities	129,780	135,435	147,211	155,535	162,192	166,668
Total Shareholders' Equity	17,756	18,170	18,253	19,610	21,726	24,189
Total Liabilities & Shareholders' Equity	147,536	153,606	165,464	175,144	183,918	190,857
RWAs	117,807	115,534	115,914	125,228	130,582	133,600

Source: Company data, QNB FS Research

Ratios/Key Indicators	2019	2020	2021	2022e	2023e	2024e
Profitability (%)						
RoTE (Attributable)	11.1	6.0	11.0	12.7	15.0	16.1
RoAA (Attributable)	1.2	0.7	1.2	1.4	1.6	1.9
RoRWA	1.5	0.9	1.7	1.9	2.3	2.6
NIM (% of IEAs)	2.45	2.40	2.77	2.88	2.93	3.07
NIM (% of RWAs)	2.56	2.66	3.20	3.38	3.49	3.71
NIM (% of AAs)	2.10	2.06	2.32	2.39	2.49	2.62
Spread	1.9	2.0	2.4	2.5	2.5	2.6
Efficiency (%)						
Cost-to-Income (Headline)	28.3	27.2	28.3	25.0	24.1	23.5
Cost-to-Income (Core)	28.7	25.7	29.1	26.0	25.3	24.6
Liquidity (%)						
LDR	115	128	120	112	114	116
LDR (Including Stable Source of Funding)	90	94	87	86	86	87
Loans/Assets	60	63	59	59	59	60
Cash & Interbank Loans-to-Total Assets	12.5	12.2	17.4	17.8	17.1	15.3
Deposits to Assets	52	49	50	52	52	52
Wholesale Funding to Loans	50	49	50	48	50	46
IEAs to IBLs (x)	1.16	1.22	1.18	1.24	1.21	1.20
Asset Quality (%)						
NPL Ratio	4.9	4.3	4.7	4.5	4.3	4.1
NPLs to Shareholders' Equity	25.3	23.8	26.2	24.9	22.8	20.7
NPL to Tier-1 Capital	26.4	23.9	25.7	25.1	24.1	23.0
Coverage Ratio	82	102	97	116	127	136
ALL/Average Loans	4.1	4.6	4.6	5.4	5.6	5.8
Cost of Risk (bps)	66	87	108	105	95	85
Capitalization (%)						
CET1 Ratio	11.1	12.2	11.7	11.6	11.9	12.6
Tier-1 Ratio	14.4	15.7	16.0	15.5	15.8	16.3
CAR	16.4	17.8	18.1	17.6	17.8	18.4
Leverage (x)	8.3	8.5	9.1	8.9	8.5	7.9
Growth (%)						
Net Interest Income	19.4	4.6	19.4	10.1	9.6	9.6
Non-Interest Income	14.0	-32.7	64.9	-1.2	5.6	3.6
Total Revenue	17.6	-7.2	29.9	6.8	8.5	8.1
Operating Expenses	4.7	-10.7	35.0	-5.7	4.5	5.6
Net Operating Income	23.6	-5.8	28.0	11.8	9.9	8.8
Net Provisions & Impairments	27.8	51.3	-11.0	-4.6	-11.6	-10.1
Net Income (Headline)	20.7	-35.6	77.1	14.8	23.7	17.2
Net Income (Attributable)	24.3	-39.6	89.6	16.8	26.4	18.8
Loans	4.0	9.9	1.3	4.6	5.3	6.9
Deposits	6.3	-0.7	8.1	11.3	4.2	5.1
Assets	9.3	4.1	7.7	5.9	5.0	3.8
RWAs	3.7	-1.9	0.3	8.0	4.3	2.3

Source: Company data, QNB FS Research

Recommendations		Risk Ratings	
<i>Based on the range for the upside / downside offered by the 12-month target price of a stock versus the current market price</i>		<i>Reflecting historic and expected price volatility versus the local market average and qualitative risk analysis of fundamentals</i>	
OUTPERFORM	Greater than +20%	R-1	Significantly lower than average
ACCUMULATE	Between +10% to +20%	R-2	Lower than average
MARKET PERFORM	Between -10% to +10%	R-3	Medium / In-line with the average
REDUCE	Between -10% to -20%	R-4	Above average
UNDERPERFORM	Lower than -20%	R-5	Significantly above average

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