

Masraf Al Rayan (MARK)

Recommendation	ACCUMULATE	Risk Rating	R-3
Share Price	QR2.360	Price Target	QR2.771
Implied Upside	17.4%	Old Price Target	QR3.112

CoR to Remain Elevated Before Normalizing in 2027; Lowering PT

Factoring in 9M2023 results, we lower our estimates for 2023, 2024 & 2025 (see page 2). Thus, our RoE estimates drop for 2023/2024. Hence, we lower our price target from QR3.112 to QR2.771 but keep our Accumulate rating. Given MARK's asset quality situation, the stock is trading at 2023e/24e P/B of 1.0x (lower than its 5-year median of 2.2x and its high of 2.5x). The stock has underperformed its peers on an YTD and 1-year TTR basis due to asset quality headwinds and RoE erosion.

Highlights

- We still expect double-digit growth in earnings; however, we lower our 2022-27e earnings CAGR from 16.8% to 14.7%:** We now estimate MARK's bottom-line to grow from 2022's QR1.26bn to QR2.51bn by 2027e (previously our 2027 estimate was QR2.74bn). The lower estimates (we have reduced our 2023-25e earnings estimate by an average of ~17%) is attributable to lower revenue and higher CoR.
- MARK's 3Q2023 net profit beat our estimates on lower provisions (revenue was in-line; variation of -2.6%).** Masraf Al Rayan reported a net profit of QR473.0mn in 3Q2023 (higher than our estimate of QR354.1mn), increasing by 42.8%/24.6% YoY/QoQ. A 35.5% drop in provisions & impairments drove YoY bottom-line. Core banking income was weak on margin compression and lower fees and f/x income.
- 9M2023 annualized RoE came in at 7.7% vs. 7.9% in 9M2022; RoE is significantly low vs. pre-merger and remains well below its CoE of 12.5%.** RoE declined from 11.3% in 2021 to 5.8% in 2022 (pre-merger RoE hovered at the 16% level). It will take a long time for RoE to pick up despite double-digit growth in earnings; thus, we lower our RoE estimates for 2023/2024 from 6.7/8.2% to 5.7/6.5%.
- Although MARK's primary exposure is to the public sector (9M2023: 47%), asset quality has faced headwinds with NPLs spiking; the bulk/majority of NPLs is attributed to the construction and real estate segments.** Pre-merger, the NPL ratio hovered around 1% but has increased to 6.47% by the end of 3Q2023 (partially due to a drop in loans). NPLs surged from QR1.92bn in FY2021 to QR7.43bn in 3Q2023. However, NPLs have been flat vs. FY2022. Moreover, Stage 2 loans as a % of total loans increased from 2021's 14% to 28% as of 3Q2023 (FY2022: 24%). At the same time, coverage of Stage 3 loans increased from 46% in FY2022 to 57% in 3Q2023.
- CoR to stay on the high side in the near-to-medium term as MARK builds buffers to reach a coverage ratio of 70% to 80% for Stage 3 loans; credit provisions moved down by 1.5% to QR927.8mn YoY in 9M2023.** CoR increased from 103bps in 9M2022 to 108bps in 9M2023. We increase our estimates of CoR from 114bps to 127bps for 2023 and 118bps from 92bps in 2024 (2025: 95bps vs. 82bps) as management increases coverage of Stage 3 loans. We expect CoR to normalize at ~86bps by 2027.
- Loans continued its negative trajectory as MARK is de-risking its loan book; we lower our gross loan growth estimates from a CAGR of 5.6% in 2022-27e to 3.4% as the bank's lending policy becomes more prudent, given its NPLs situation.** Net loans decreased by 1.7% QoQ to QR109.9bn (-6.7% vs. FY2022). On the other hand, deposits increased by 4.1% sequentially to QR92.5bn (-4.9% vs. FY2022).
- CET1 to remain robust and highest among its peers.** MARK ended 3Q2023 with CET1/Tier-1 ratios of 19.6%/20.6%. Going forward, we expect capitalization to hover around current levels.

Catalysts

- 1) Normalizing CoR, which results in strong RoE ahead of expectations.

Recommendation, Valuation and Risks

- Recommendation and valuation: We lower our PT from QR3.112 to QR2.771/share, but maintain our Accumulate rating.** MARK is trading at 2023e/24e P/TB of 1.0x and P/E 17.9x/15.6x.
- Risks:** 1) Geopolitical factors & 2) Greater-than-expected increase in credit costs.

Key Financial Data and Estimates

	2022	2023e	2024e	2025e
EPS Attributable (QR)	0.136	0.132	0.152	0.194
EPS Growth (%)	-22.4	-3.0	15.2	27.6
P/E (x)	17.4	17.9	15.6	12.2
Tangible BVPS (QR)	2.30	2.33	2.38	2.43
P/TBV (x)	1.0	1.0	1.0	1.0
RoE (%)	5.8	5.7	6.5	8.1
DPS (QR)	0.100	0.100	0.150	0.175
Dividend Yield (%)	4.2	4.2	6.4	7.4

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

Key Data

Current Market Price (QR)	2.360
Dividend Yield (%)	4.2
Bloomberg Ticker	MARK QD
ADR/GDR Ticker	N/A
Reuters Ticker	MARK.QA
ISIN	QA000A0M8VM3
Sector*	Banks & Fin. Svcs.
52wk High/52wk Low (QR)	3.838/1.890
3-m Average Volume (mn)	1,725.5
Mkt. Cap. (\$ bn/QR bn)	6.0/21.9
Shares Outstanding (mn)	9,300
FO Limit* (%)	100.0
Current FO* (%)	14.8
1-Year Total Return (%)	(35.7)
Fiscal Year End	December 31

Source: Bloomberg (as of November 12, 2023), *Qatar Exchange (as of November 12, 2023); Note: FO is foreign institutional ownership

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Change in Estimates

In QR mn	2023e			2024e			2025e		
	Old	New	Change (%)	Old	New	Change (%)	Old	New	Change (%)
Net Interest Income	3,528	3,001	-14.9	3,611	3,217	-10.9	3,799	3,452	-9.1
Non Interest Income	756	766	1.3	793	732	-7.7	871	792	-9.0
Revenue	4,284	3,767	-12.1	4,404	3,949	-10.3	4,670	4,244	-9.1
Opex	(1,143)	(979)	-14.4	(1,141)	(1,013)	-11.2	(1,219)	(1,077)	-11.7
Net Operating Income	3,141	2,788	-11.2	3,263	2,935	-10.0	3,451	3,167	-8.2
Net Income (Reported)	1,508	1,303	-13.6	1,886	1,494	-20.8	2,276	1,893	-16.8
Net Income (Attributable)	1,414	1,224	-13.4	1,793	1,410	-21.3	2,173	1,800	-17.2

Source: QNB FS Research

Valuation

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

We derive MARK's fair value by employing the RI valuation technique (based on a fundamental P/B).

We add Qatar's 10-year CDS rate of 0.91% to the 10-year US government bond yield (4.8%) to arrive at a risk free rate of 5.7%. We factor in an adjusted beta of 0.97x. Finally, we add a local equity risk premium of 7.0% to arrive at a Ke of 12.52%. However, we use a Ke of 10.0% for the terminal year.

Valuation Methodology

Fundamental P/B	RI Based on Fundamental P/B	
Sustainable RoE (%)	13.5	
Estimated Cost of Equity (%)	10.0	
Terminal Growth Rate (%)	5.0	
Fundamental P/B	1.7x	
	Beginning BVPS (2023) (QR)	2.48
	Present Value of Interim Residuals (QR)	(0.47)
	Present Value of Terminal Value (QR)	0.87
	Less: 30% of NPLs	(0.24)
	Fundamental P/B	1.7x
	Intrinsic Value (QR)	2.771
	Current Market Price (QR)	2.360
	Upside/(Downside) Potential (%)	+17.4%

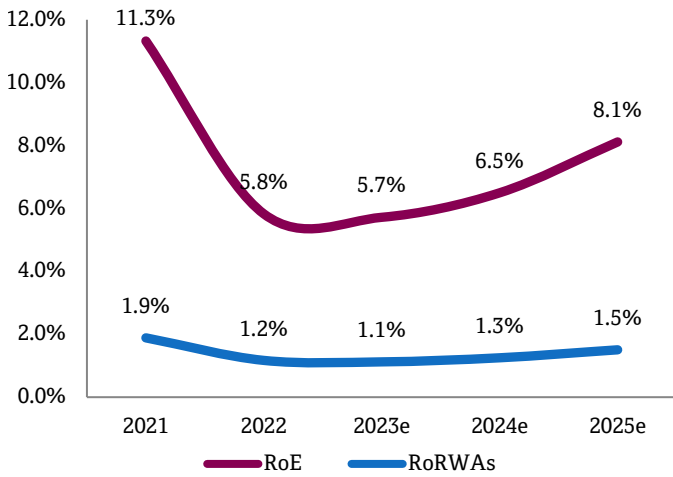
Source: QNB FS Research

Forecasts

	2023e	2024e	2025e	2026e	2027e	2028e	2029e	2030e	2031e	Terminal
Beginning BVPS	2.48	2.51	2.57	2.61	2.65	2.72	2.83	2.93	3.02	3.10
Attributable EPS	0.13	0.15	0.19	0.22	0.27	0.30	0.33	0.36	0.39	0.42
DPS	0.10	0.10	0.15	0.175	0.200	0.200	0.225	0.275	0.300	0.325
Adjustment	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Ending BVPS	2.51	2.57	2.61	2.65	2.72	2.83	2.93	3.02	3.10	3.20
Equity Charge	0.31	0.31	0.32	0.33	0.33	0.34	0.35	0.37	0.38	0.31
Residual Income	-0.18	-0.16	-0.13	-0.11	-0.06	-0.04	-0.02	-0.01	0.01	0.11
Terminal Value (Based on Fundamental P/B)										2.24
Discounted Interim Residuals	-0.16	-0.13	-0.09	-0.07	-0.03	-0.02	-0.01	0.00	0.00	0.04
Discounted Terminal Value										0.87

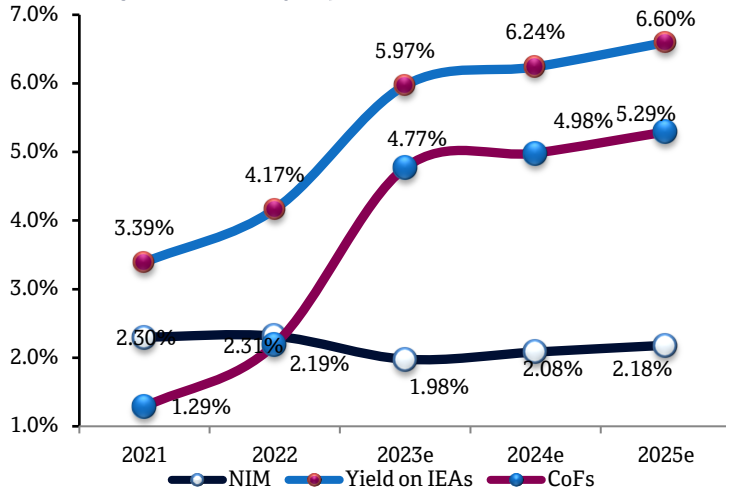
Source: QNB FS Research

RoE & RoRWAs to Steadily Improve; RoE to Remain < CoE

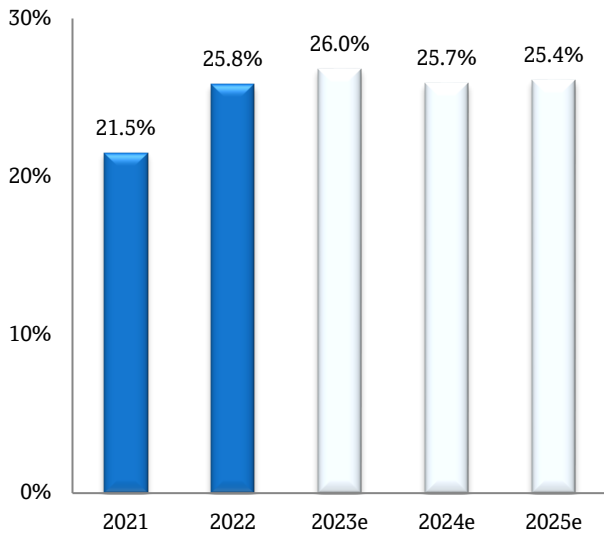


Source: Company data, QNB FS Research

While Margins to Gradually Improve

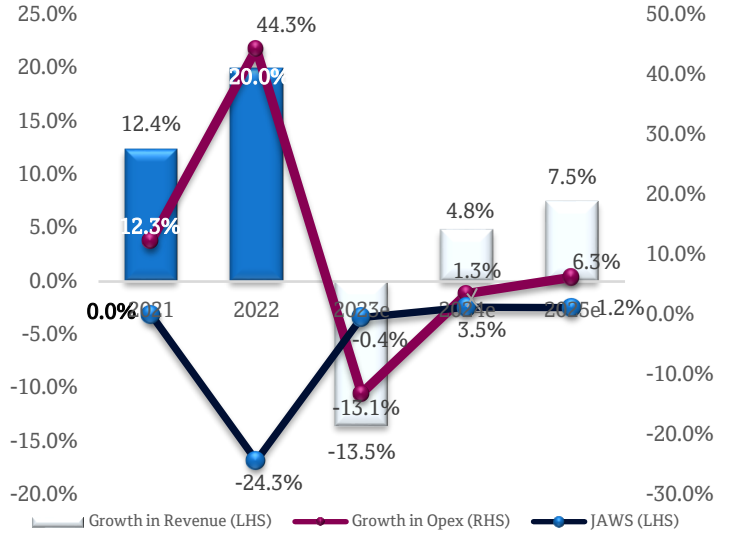


C/I Ratio to Remain at Current Levels Due to Cost Containment

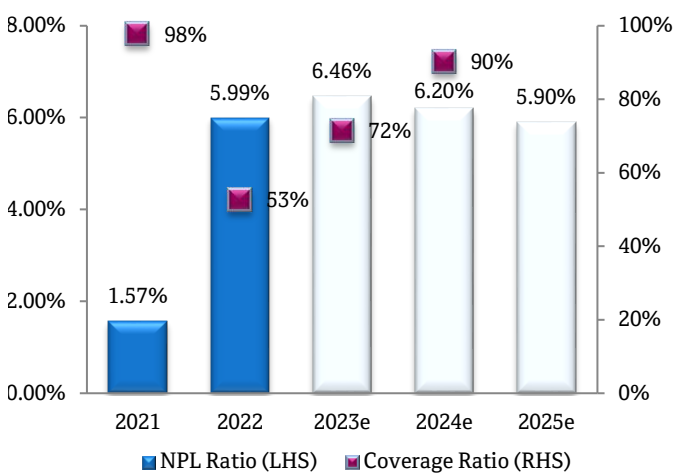


Source: Company data, QNB FS Research; 2021 & 2022 C/I excludes one-time integration costs

While Generating Negative-to-Neutral JAWS



NPL Ratio Spiked on The Back of Contracting & Real Estate Loans



Source: Company data, QNB FS Research

Coverage of Stage 3 Loans (NPLs) Improved to 57% from 46%

3Q2023	Stage 1	Stage 2	Stage 3	Total
Gross Loans	74,874,549	32,495,814	7,433,032	114,803,395
ALLs	34,844	562,375	4,258,819	4,856,038
Stages % Loans	65.2%	28.3%	6.47%	-
Coverage Ratio	0.05%	1.73%	57%	-

Detailed Financial Statements

Income Statement (In QR mn)	2021	2022	2023e	2024e	2025e	2026e
Net Interest Income	3,113	3,607	3,001	3,217	3,452	3,811
Fees & Commissions	324	432	423	467	523	487
FX Income	173	271	163	195	209	227
Other Income	19	46	181	69	60	58
Non-Interest Income	516	748	766	732	792	772
Total Revenue	3,629	4,355	3,767	3,949	4,244	4,584
Operating Expenses	(780)	(1,126)	(979)	(1,013)	(1,077)	(1,142)
Net Operating Income	2,849	3,229	2,788	2,935	3,167	3,441
Net Provisions & Impairments	(1,097)	(1,710)	(1,418)	(1,388)	(1,206)	(1,225)
Net Profit Before Taxes & Minority Interest	1,752	1,519	1,371	1,547	1,961	2,216
Tax	(5)	(22)	(41)	(23)	(29)	(33)
Net Profit Before Minority Interest	1,747	1,497	1,329	1,524	1,932	2,183
Minority Interest	(13)	(19)	(27)	(30)	(39)	(44)
Non-Recurring Items	(16)	(134)	-	-	-	-
Net Profit (Reported/Headline)	1,718	1,344	1,303	1,494	1,893	2,139
Interest Expense on AT1 Bond	(48)	(46)	(46)	(46)	(46)	(46)
Social & Sports Contribution Fund	(43)	(36)	(33)	(37)	(47)	(53)
Net Profit (Attributable)	1,627	1,263	1,224	1,410	1,800	2,039

Source: Company data, QNB FS Research

Balance Sheet (In QR mn)	2021	2022	2023e	2024e	2025e	2026e
Assets						
Cash & Balances with Central Bank	5,221	5,088	5,110	5,572	6,072	6,436
Interbank Loans	9,156	6,109	6,370	5,652	6,478	6,203
Net Investments	32,753	31,477	36,899	41,115	34,979	36,568
Net Loans	120,880	117,859	109,821	113,037	117,779	124,053
Investment In Associates	349	346	369	380	390	397
Other Assets	3,280	4,074	4,057	4,076	3,945	4,020
Net PP&E	715	902	976	1,039	1,088	1,139
Goodwill & Intangibles	1,802	1,679	1,679	1,679	1,679	1,679
Total Assets	174,155	167,533	165,280	172,550	172,409	180,494
Liabilities						
Interbank Deposits	23,247	28,805	24,617	26,225	18,876	19,462
Customer Deposits	106,956	97,292	98,265	103,178	110,400	117,024
Sukuks & Borrowings	13,436	11,525	12,332	12,332	12,332	12,332
Other Liabilities	5,850	5,629	5,463	5,701	5,243	5,663
AT1 Notes	1,000	1,000	1,000	1,000	1,000	1,000
Total Liabilities	150,488	144,251	141,677	148,436	147,852	155,482
Minority Interest	200	198	225	255	294	338
Total Shareholders' Equity	23,467	23,084	23,378	23,858	24,263	24,675
Total Liabilities & Shareholders' Equity	174,155	167,533	165,280	172,550	172,409	180,494

Source: Company data, QNB FS Research

Ratios/KPIs	2021	2022	2023e	2024e	2025e	2026e
Profitability (%)						
RoE	11.3	5.8	5.7	6.5	8.1	9.0
RoAA	1.1	0.7	0.7	0.8	1.0	1.2
RoRWA	1.9	1.2	1.1	1.3	1.5	1.6
NIM (% of IEAs)	2.30	2.31	1.98	2.08	2.18	2.36
NIM (% of RWAs)	3.61	3.34	2.75	2.86	2.89	3.06
NIM (% of AAs)	2.11	2.11	1.80	1.90	2.00	2.16
Spread	2.1	2.0	1.2	1.3	1.3	1.4
Efficiency (%)						
Cost-to-Income (Headline)	21.5	25.8	26.0	25.7	25.4	24.9
Cost-to-Income (Core)	21.6	26.0	26.6	26.0	25.7	25.2
Liquidity (%)						
LDR (Loans to Stable Sources of Funds)	100	108	99	98	96	96
Loans/Assets	69.4	70.3	66.4	65.5	68.3	68.7
Cash & Interbank Loans-to-Total Assets	8.3	6.7	6.9	6.5	7.3	7.0
Deposits to Assets	61.4	58.1	59.5	59.8	64.0	64.8
Wholesale Funding to Loans	30.3	34.2	33.6	34.1	26.5	25.6
IEAs to IBLs	118.1	118.9	120.0	119.7	120.0	119.7
Asset Quality (%)						
NPL Ratio	1.57	5.99	6.46	6.20	5.90	5.50
NPL to Shareholders' Equity	8.19	31.60	31.98	31.28	30.72	29.84
NPL to Tier 1 Capital	9.04	33.70	32.66	31.29	29.87	28.25
Coverage Ratio	97.8	52.7	71.5	90.3	106.6	124.7
ALL/Average Loans	1.7	2.6	4.2	5.3	5.9	6.5
Cost of Risk (bps)	87	127	127	118	98	95
Capitalization (%)						
CET1 Ratio	19.4	18.6	20.5	19.3	19.9	19.6
Tier-1 Ratio	20.3	19.5	21.4	20.2	20.7	20.3
CAR	21.2	20.3	22.3	21.1	21.6	21.2
Leverage (x)	7.4	7.3	7.1	7.2	7.1	7.3
Growth (%)						
Net Interest Income	12.4	15.9	-16.8	7.2	7.3	10.4
Non-Interest Income	11.9	45.1	2.4	-4.5	8.3	-2.5
Opex	12.3	44.3	-13.1	3.5	6.3	6.1
Net Operating Income	12.4	13.4	-13.7	5.3	7.9	8.6
Net Income (Reported)	-21.0	-21.7	-3.1	14.6	26.8	13.0
Net Income (Attributable)						
Loans	40.2	-2.5	-6.8	2.9	4.2	5.3
Deposits	55.2	-9.0	1.0	5.0	7.0	6.0
Assets	43.7	-3.8	-1.3	4.4	-0.1	4.7
RWAs	54.8	6.1	-3.7	10.5	2.1	6.2

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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