Alinma Bank
Investment Update

الجزيرة كابيتال
ALJAZIRA CAPITAL الجزيرة للأسواق المالية

NIMs to decline as rates come down; Trading at 2024E PB of 2.4x positives are in the price

Alinma posted in-line with expectations earnings in Q2-24, logging in the highest ever funded income driven by the robust expansion in loan book (+17.4% Y/Y). The bank has experienced a 37bps and 612bps improvement in NIMs and ROE since the start of interest rate increases in 2022. In the impending rate downcycle, we see NIMs to remain largely unchanged in 2024 and decline by -21/10bps Y/Y to 3.47/3.37% in 2025/26E. The aforementioned reversal in NIMs is owed to the assets/liabilities duration mismatch (60.0% of assets reprice within one year, as compared to 54.1% of liabilities). We expect loan growth to remain in high teens in 2024, and see moderation in cost of risk to 69bps (due to high coverage). ROEs are estimated to contract by 26bps to 17.23% in 2025, following a 109bps increase in 2024. We forecast EPS to grow by 18.8/10.3% to SAR 2.21/2.43 per share, and DPS to stand at SAR 0.75/1.0 per share (DY 2.4/3.2%) in 2024/25, respectively. At 2024E PB of 2.4x we believe positives are in the price, hence we see limited room for re-rating of the stock. We maintain our "Neutral" recommendation, with revised up TP of SAR 35.5/share.

Alinma posts in-line with expectations results in Q2-24; logs in highest ever funded income due to robust asset growth: Alinma bank posted earnings of SAR 1.42bn in Q2-24, up 15.6% Y/Y (+7.7% sequentially), the result was inline with AJC estimates (+6.0% deviation). The deviation was driven by stronger than expected growth in loans (+17.4% Y/Y) and better performance on net interest margins front (-4bps Y/Y). Net Special Commission Income grew by 15.7% Y/Y in Q2-24 (+5.8% deviation from AJC estimate) due to 17.4% and 16.2% Y/Y increase in loans and investments. Non-Commission Income improved by 3.1% Y/Y (+6.2% deviation from AJC estimate). Operating expenses (excluding debt provisions) totaled at SAR 834mn, up 11.7% Y/Y (+0.1% on Q/Q basis), in line with our estimates (+3.8% deviation). A relatively smaller increase in opex as compared to operating income, caused the cost to income ratio to drop by 26bps Y/Y to 30.4% in Q2-24. Provision expenses grew by 0.4% Y/Y to SAR 327mn (+23.5% on a Q/Q basis), 8.9% above our estimate of SAR 300mn. NPL ratio saw a 111bps Y/Y drop to 0.78% in Q2-24, while coverage improved by 110ppts to 240.1%. The sharp increase in coverage and improvement in NPL ratio is owed the SAR 1.4bn write offs booked during 1H-24. Loan book expanded by 17.4% Y/Y & 5.1% Q/Q to SAR 189.9bn in Q2-24; retail loans grew by 9.3% Y/Y while corporate loans increased by 20.1% Y/Y. ADR ratio increased to 92.5% in Q2-24 from 90.9% in Q2-23 (95.6% in Q1-24), as loan growth outpaced deposit growth. Moreover, the bank expanded its investments book by 16.2% Y/Y (+2.9% on a Q/Q basis) to SAR 46.6bn. CAR improved by 10bps Y/Y to 18.5% in Q2-24.

NIMs to undergo a sizable decline over the next two years as Fed lowers interest rates; ROE to undergo some attrition in 2025: According to CME FedWatch, there is 100% probability that FED will cut interest rates by atleast 25bps in Sept-24 (probability of 50bps cut is 32.5%). We expect two 25bps cuts in 2024 and four quarter point cuts in 2025. In this backdrop, due to assets/liabilities duration mismatch (60.0% of assets reprice within one year, as compared to 54.1% of liabilities), we expect Alinma to see a notable decline in NIMs, -21/10bps to 3.47/3.37% in 2025/26E, respectively. Overall, we forecast Return on Earning Assets to decline by 97bps Y/Y in 2025, while we forecast 145bps Y/Y drop in the cost of remunerative liabilities. We expect bank to see a 36bps decline in ROE in 2025 to 17.2%, mainly driven by 21bps Y/Y decline in NIMs. Net income growth is estimated to slowdown to 10.3% Y/Y in 2025, following 18.8% Y/Y increase in 2024 (2023-27E CAGR 13.7%). Net income from investment and financing activities is expected to stand at 14.5/9.2% Y/Y (2023-27E CAGR 11.4%), while non-funded income is expected to increase by 13.9/10.3% Y/Y in 2024/25 (2023-27E CAGR 10.7%).

Recommendation	Neutral
Target Price (SAR)	35.5
Upside / (Downside)*	12.7%

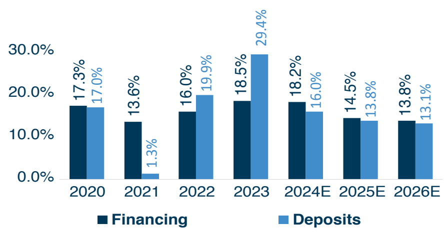
Source: Tadawul *prices as of 17th of August 2024

Key Financials

in SAR mn, (unless specified)	FY22	FY23	FY24E	FY25E
Net financing & investment income	6,066	7,655	8,764	9,572
Growth %	18.1%	26.2%	14.5%	9.2%
Net Profit	3,441	4,639	5,513	6,083
Growth %	32.1%	34.8%	18.8%	10.3%
EPS	1.38	1.86	2.21	2.43
DPS	0.75	0.75	0.75	1.00

Source: Company reports, Aljazira Capital

Fig 1: Loans and Deposit Growth



Source: Company reports, Aljazira Capital

Key Ratios

	FY22	FY23	FY24E	FY25E
NIMs	3.5%	3.8%	3.7%	3.5%
P/E (x)	22.6	17.0	14.3	12.9
P/B (x)	3.0	2.7	2.4	2.1
Dividend Yield	2.4%	2.4%	2.4%	3.2%
ROA	1.8%	2.1%	2.1%	2.0%
ROE	12.9%	16.5%	17.6%	17.2%
Net loan growth	16.0%	18.5%	18.2%	14.5%
Deposit growth	19.9%	29.4%	16.0%	13.8%

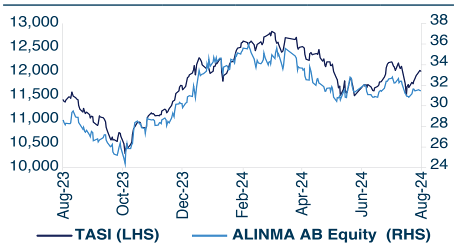
Source: AlJazira Capital, Company accounts

Key Market Data

Market Cap (SAR bn)	78.8
YTD%	2.04%
52 week (High)/(Low)	36/24.2
Share Outstanding (mn)	2500

Source: Company reports, Bloomberg, Aljazira Capital

Price Performance



Source: Tadawul, Aljazira Capital

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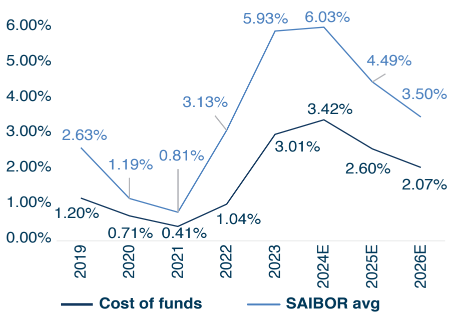
Loan growth guidance revised up to high-teens from earlier expectation of mid-teen growth: In the Q1-24 investor presentation the bank management guided for loan growth to remain in mid-teens in 2024. However, Alinma has revised up 2024 loan growth expectation to high teens in Q2-24 investor briefing. The bank expects strong growth in mid-corporate, SME & retail and sustained growth in corporate loan book. Overall loan growth stood at 17.4% Y/Y in Q2-24 (5.1% Q/Q) and outstanding loans reached SAR 189.9bn, retail loans grew by 9.3% Y/Y while corporate loans increased by 20.1% Y/Y. We forecast loan growth to stand at 18.2/14.5% in 2024/25, driven by strong demand from corporate and project financing, due to mega/giga projects and declining interest rates. Deposits grew by 15.5% Y/Y to SAR 205.4bn and share of demand deposits in total deposits increased by 146bps Y/Y. We expect the deposit growth to stand at 16% Y/Y in 2024 and decline to 13.8% in 2025.

Funding costs to see stronger decline in the forthcoming rate down cycle, as compared to 2019 rate cuts, due to higher share of rate sensitive deposits: Alinma has seen a notable increase in share of remunerative deposits over the last four years as the bank sizably grew its loan book; interest bearing deposits have increased to 55.9% of total deposits as of Q2-24 from 43.2% of total deposits in Q4-19. This increase has made the cost of funding more sensitive to changes in interest rates, hence we see a larger decline in cost of funds in current rate downcycle as compared to the rate cuts made in 2019. Overall, we forecast Cofs to decline by 82/53bps in 2025/26.

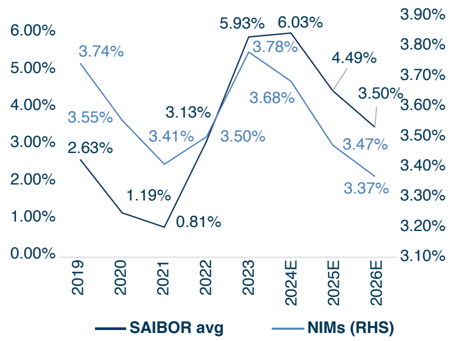
Bank revises guidance on asset quality, capital adequacy and operational effeciency in Q2-24: Apart from loan growth, bank has revised three key variables in Q2-24 investor presentation. Firstly the management expects cost of risk to see some moderation due to better coverage, and remain in the 60-70bps range in 2024 as compared to previous range of 65-75bps. Secondly CAR is expected to stay around 18-19% against previous expectation of 19-20% (this downwards revision could be due to upwards revision in asset growth guidance). Lastly Alinma has revised up cost to income ratio to 31% from 30%, due to strategic investments. We expect cost of risk to remain at 69bps, CAR to clock in around 18% and Cost to income ratio remain at 31% in 2024.

Fig 2: CoFs to see steeper decline



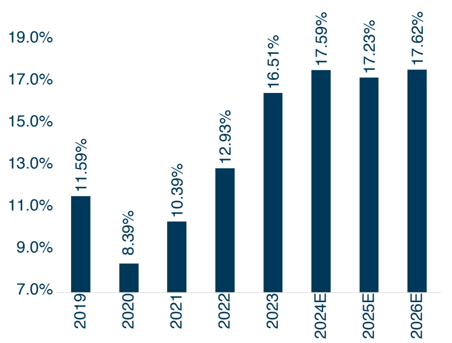
Source: Aljazira capital Research, Company accounts

Fig 3: NIMs to shrink as rates come down



Source: Aljazira capital Research, Company accounts

Fig 4: ROE to edge down in 2025



Source: Aljazira capital Research, Company accounts

Investment thesis and valuation:

Alinma has experienced a 37bps and 612bps improvement in NIMs and ROE since the beginning of interest rate increases in 2022, thanks to the heavy exposure in floating rate corporate loans. Due to shorter asset duration, we foresee a notable decline in margins in the medium term as rates start coming down from peak levels. We forecast Alinma to deliver medium term (2023-27) earnings CAGR of 13.7%. We forecast EPS to grow by 18.8/10.3% to SAR 2.21/2.43 per share, and DPS to stand at SAR 0.75/1.0 per share (DY 2.4/3.2%) in 2024/25, respectively. Trading at 2024E PB of 2.4x, we believe positives are in the price, hence we see limited room for re-rating of the stock.

We value the stock based on equal weight to Residual Income and Two staged Gordon growth. Our residual income-based TP assuming the cost of equity of 11.7% is SAR 35.7 per share whereas; through the Two staged Gordon growth model, based on ROE of 17.2%, we arrive at a justified P/B multiple of 2.4x. Hence, the equal weight revised up TP stands at **SAR 35.5 per share** which translates to an upside of 12.7% from the CMP of SAR 31.5 per share, hence we maintain our "**Neutral**" recommendation.

Weighted Average TP

Method	Value	Weight	W.Value
RI	35.70	50%	17.85
Justified P/B	35.29	50%	17.64
Price Target			**35.50**
Upside/Downside			12.7%

Source: Aljazira capital Research, Company accounts

Key Financials

Amount in USD mn, unless otherwise specified	FY20	FY21	FY22	FY23	FY24E	FY25E	FY26E	FY27E	FY28E
Income statement									
Net financing and investments income	4,648	5,137	6,066	7,655	8,764	9,572	10,583	11,772	13,092
Fees from banking services, net	936	1,085	1,209	1,459	1,710	1,917	2,133	2,342	2,540
Exchange income, net	220	215	291	330	347	364	382	401	421
Dividend and other operating income	(122)	230	397	282	292	303	315	327	340
Total operating income	5,682	6,667	7,963	9,726	11,113	12,155	13,412	14,842	16,393
Impairment charge for financing	(1,419)	(1,252)	(1,198)	(1,272)	(1,312)	(1,520)	(1,605)	(1,813)	(2,024)
Other operating expenses	(2,065)	(2,380)	(2,756)	(3,070)	(3,443)	(3,643)	(3,835)	(4,008)	(4,157)
Operating Profit	2,197	3,036	4,010	5,384	6,358	6,993	7,972	9,021	10,212
Y/Y	**-22.3%**	**38.2%**	**32.1%**	**34.3%**	**18.1%**	**10.0%**	**14.0%**	**13.2%**	**13.2%**
Share of loss from associate	5	(14)	4	12	12	12	12	12	12
Zakat	(236)	(312)	(414)	(556)	(657)	(722)	(823)	(931)	(1,054)
Net income	1,966	2,709	3,599	4,839	5,713	6,283	7,160	8,101	9,170
Y/Y	**-22.4%**	**37.8%**	**32.8%**	**34.4%**	**18.1%**	**10.0%**	**14.0%**	**13.1%**	**13.2%**
Net income (adjusted for Tier-1)	1,966	2,659	3,441	4,639	5,513	6,083	6,960	7,901	8,970
EPS	**0.79**	**1.08**	**1.44**	**1.94**	**2.29**	**2.51**	**2.86**	**3.24**	**3.67**
EPS (adujusted for Tier-1)	**0.79**	**1.33**	**1.38**	**1.86**	**2.21**	**2.43**	**2.78**	**3.16**	**3.59**
DPS	**0.25**	**0.50**	**0.75**	**0.75**	**0.75**	**1.00**	**1.00**	**1.25**	**1.25**
Balance sheet									
Assets									
Cash and balances with SAMA	12,208	9,177	9,723	12,598	14,612	16,635	18,819	21,023	23,210
Due from banks and other financial institutions	443	738	1,454	1,701	1,973	2,246	2,541	2,838	3,134
Investments, net	29,526	33,278	38,529	43,236	50,145	57,088	64,585	72,149	79,654
Financing, net	111,196	126,271	146,492	173,624	205,181	234,836	267,195	300,119	333,083
Property and equipment, net	2,365	2,383	2,633	2,888	3,177	3,495	3,844	4,229	4,651
Other assets, net	1,139	1,629	1,605	2,667	2,800	2,941	3,088	3,242	3,404
Total assets	156,877	173,476	200,436	236,715	277,888	317,240	360,072	403,600	447,136
Liabilities & owners' equity									
Due to banks and other financial institutions	7,312	15,240	16,483	7,431	9,307	12,912	16,755	20,223	23,098
Customers' deposits	119,454	121,061	145,168	187,901	217,925	248,099	280,681	313,552	346,168
Amount due to Mutual Funds' unitholders	110	496	137	94	94	94	94	94	94
Other liabilities	5,571	5,969	6,772	6,956	8,471	10,126	12,029	14,109	16,356
Share capital	20,000	20,000	20,000	20,000	25,000	25,000	25,000	25,000	25,000
Statutory reserve	591	1,269	2,169	3,378	4,757	6,277	8,018	9,993	12,235
Net change in fair value of 'available for sale' investments	-	-	-	-	-	-	-	-	-
Other reserves	177	155	(507)	62	62	62	62	62	62
Retained earnings	3,760	3,586	4,285	1,118	3,747	6,144	8,908	12,041	15,598
Proposed issue of bonus shares	-	-	-	5,000	-	-	-	-	-
Proposed gross dividend	-	795	996	-	-	-	-	-	-
Treasury shares	(100)	(94)	(66)	(226)	(226)	(226)	(226)	(226)	(226)
Tier 1 Sukuk	-	5,000	5,000	5,000	8,751	8,751	8,751	8,751	8,751
Total shareholders' equity	24,429	30,711	31,876	34,334	42,091	46,009	50,514	55,622	61,421
Total equity & liabilities	156,877	173,476	200,436	236,715	277,888	317,240	360,072	403,600	447,136
Key fundamental ratios									
Capital Ratios									
Equity/ Total Assets	16%	18%	16%	15%	15%	15%	14%	14%	14%
Tier 1 ratio	18%	22%	19%	16%	17%	16%	16%	15%	15%
Total (Tier 1 and Tier 2 ratio)	19%	23%	20%	17%	18%	17%	16%	16%	16%
Profitability Ratios									
NIMs	3.6%	3.4%	3.5%	3.8%	3.7%	3.5%	3.4%	3.3%	3.3%
Return On Assets (ROA)	1.4%	1.6%	1.8%	2.1%	2.1%	2.0%	2.1%	2.1%	2.1%
Return On Equity (ROE)	8.4%	10.4%	12.9%	16.5%	17.6%	17.2%	17.6%	17.8%	18.0%
ROE/ROA (Leverage Ratio) (X)	6.2	6.6	7.0	7.8	8.2	8.4	8.6	8.6	8.5
Asset Quality Ratios									
NPL ratio	2.5%	1.8%	1.9%	1.6%	0.8%	0.8%	0.8%	0.8%	0.8%
NPL Coverage	114%	177%	136%	155%	250%	246%	237%	230%	227%
Funding Ratios									
Loans/ Customer Deposits	93.1%	104.3%	100.9%	92.4%	94.2%	94.7%	95.2%	95.7%	96.2%
Liquid Assets / Total Assets	97.8%	97.7%	97.9%	97.7%	97.8%	98.0%	98.1%	98.1%	98.2%
Net Loans / Total Assets	70.9%	72.8%	73.1%	73.3%	73.8%	74.0%	74.2%	74.4%	74.5%
Market/valuation ratios									
DPS	0.25	0.50	0.75	0.75	0.75	1.00	1.00	1.25	1.25
Dividend Yield	1.5%	2.1%	2.3%	2.4%	2.4%	3.2%	3.2%	4.0%	4.0%
Book Value Per Share (BVPS)	9.8	10.3	10.8	11.7	13.3	14.9	16.7	18.7	21.1
Market price	16.3	24.0	32.6	31.5	31.5	31.5	31.5	31.5	31.5
PE (x)	20.7	22.1	22.6	17.0	14.3	12.9	11.3	10.0	8.8
PB (x)	1.7	2.3	3.0	2.7	2.4	2.1	1.9	1.7	1.5
Growth rates									
Investments (Y/Y)	25.8%	12.7%	15.8%	12.2%	16.0%	13.8%	13.1%	11.7%	10.4%
Financing (Y/Y)	17.3%	13.6%	16.0%	18.5%	18.2%	14.5%	13.8%	12.3%	11.0%
Deposits (Y/Y)	17.0%	1.3%	19.9%	29.4%	16.0%	13.8%	13.1%	11.7%	10.4%

Sources: AlJazira Capital, Company accounts

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RATING TERMINOLOGY

1. Overweight: This rating implies that the stock is currently trading at a discount to its 12 months price target. Stocks rated "Overweight" will typically provide an upside potential of over 10% from the current price levels over next twelve months.
2. Underweight: This rating implies that the stock is currently trading at a premium to its 12 months price target. Stocks rated "Underweight" would typically decline by over 10% from the current price levels over next twelve months.
3. Neutral: The rating implies that the stock is trading in the proximate range of its 12 months price target. Stocks rated "Neutral" is expected to stagnate within +/- 10% range from the current price levels over next twelve months.
4. Suspension of rating or rating on hold (SR/RH): This basically implies suspension of a rating pending further analysis of a material change in the fundamentals of the company.

Disclaimer