



WEALTH MANAGEMENT

## STOCK OF THE MONTH

May 2013

KUWAIT

BANKING SECTOR

### Recommendation

**BUY**

CMP (KWd) (15-May-13) : 590  
TARGET PRICE (KWd) : 665  
EXPECTED RETURN (%): 12.7%

### STOCK DATA

MCAP (KWd million)	3.34
52 WEEK HIGH (KWd)	0.600
52 WEEK LOW (KWd)	0.570

### ANALYST

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## BURGAN BANK SAK (KSE: BURG)

*Exposure to high growth markets, domestic expansion and consolidation of newly acquired subsidiary to drive growth*

### KEY HIGHLIGHTS

- ✦ Burgan Bank is Kuwait's fourth largest bank by assets and has a market share of 9%. The bank has subsidiaries in Algeria, Tunisia, Jordan and Iraq which comprise of 40% of its total assets. In December 2012, Burgan Bank completed the acquisition of a 99.3% stake in Turkish bank Eurobank Tefken (renamed Burgan Bank Turkey effective January 28, 2013) which is expected to add significant value to Burgan bank's earnings in 2013.
- ✦ The Central Bank of Kuwait foresees a dramatic slowdown in the country's economic growth to 1.9% for 2013 on expectations of a reduction in crude output which will adversely affect oil revenues for the year. Kuwait witnessed growth of 6.2% in 2012 and 8.2% in 2011.
- ✦ Commercial banks in Kuwait may see a sluggish credit growth during the year the government reduces spending. Credit growth in Kuwait's banks came at 5% year-on-year at the end of 2012 and grew 1.4% sequentially at the end of Q1 2013.
- ✦ The Kuwait government reported a budget surplus of KWD 17.2 billion in the first ten months of this fiscal year ending March 31, 2013 primarily on account of lower spending, which was less than half of the KWD 21.2 billion spending earmarked in the budget.
- ✦ Despite the above mentioned challenges, we recommend Burgan Bank on account it's diversified asset base which is spread among other fast growing economies such as Algeria, Turkey and Iraq. The IMF forecasts real GDP growth in Turkey at 3.4% in 2013 while Algeria and Iraq are expected to grow 3.3% and 9% in 2013 respectively. In contrast, real GDP growth for Kuwait in 2013 is projected at 1.1%.

### SHAREHOLDING PATTERN

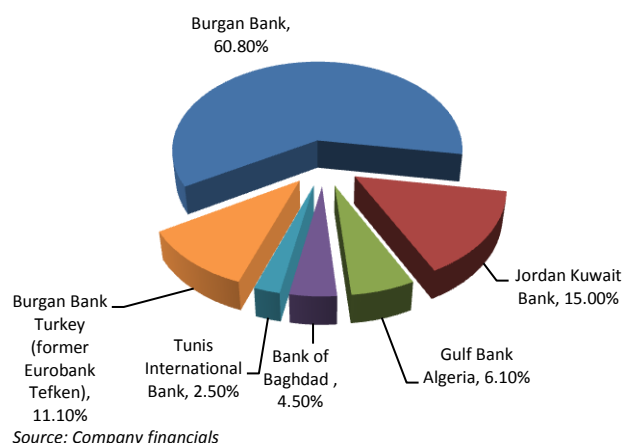
Name	%
Kuwait Projects Company (KIPCO)	41%
United Gulf Bank	17%
Wafra Investment	8%

Source: Company financials

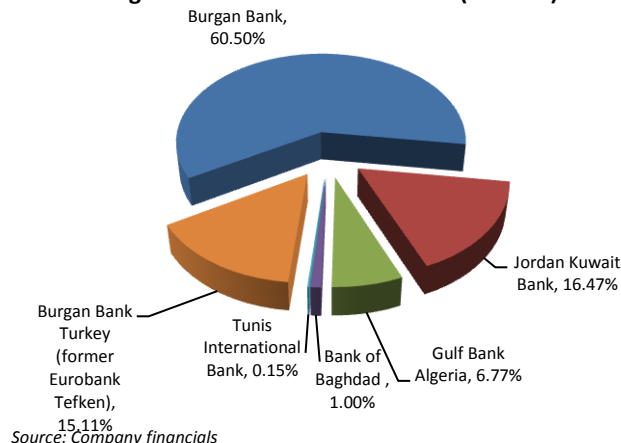
## EARNINGS OUTLOOK AND VALUATION

- ✦ Burgan Bank reported a 16% year-on-year growth in net income in Q1 2013 to KWD 20.4 million (excluding KWD 5 million of precautionary provisions). Operating profit improved 12% year-on-year to KWD 29.8 million. Provisioning during the quarter was 52% lower quarter-on-quarter and 18% higher year-on-year despite the precautionary provision.
- ✦ We expect Burgan Bank to witness a 30% year-on-year growth in total operating income to KWD 245 million in FY 2013 and 33% year-on-year growth in net income to KWD 75 million on account of the bank's exposure to high-growth markets such as Algeria and Turkey. In addition the bank should also benefit from the ongoing expansion of its retail operations in its domestic market.
- ✦ With regards to asset quality, we believe credit costs have likely peaked at 11.5% in FY 2011, and should start retreating from current levels.
- ✦ This stock trades at 1.64 times 2013E book value per share of KWD 0.360 which is at a 9% discount to its historical average P/BV since 2006. In addition, we believe the stock is trading at attractive levels given its historical valuation band between 1.44 times and 2.38 times. We value this stock at 1.85 times its FY 2013E book value, which works out to a fair value of KWD 0.665.
- ✦ Downside risk to our expectations could emerge in case asset quality weakens or cost of risk increases which could adversely affect margins. Burgan Bank is also exposed to country-specific risks in each of the markets where it operates, including political uncertainties in markets such as Tunisia, Iraq.
- ✦ Burgan Bank recorded an 8.9% year-on-year growth in consolidated net profit at KWD 62.7 million in 2012 driven by 13.7% year-on-year increase in net interest income and a 21% year-on-year increase in other operating income. The Groups loan book expanded 50% year-on-year while customer deposits grew 39% year-on-year while loans to deposit ratio stood at 89%.

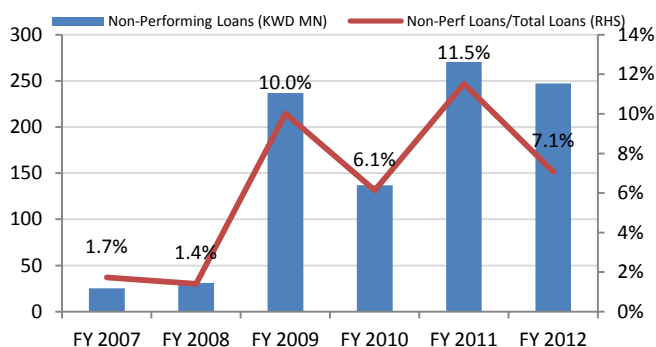
**Burgan Bank Distribution of Assets (FY 2012)**



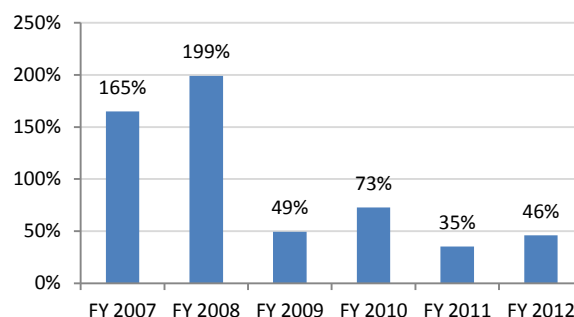
**Burgan Bank Distribution of Loans (FY 2012)**



- ✦ The Group's asset quality improved in FY 2012 as NPL's ratio declined to 7.1% from 11.5% in FY 11 while provisions coverage ratio increased to 46% at the end of 2012.

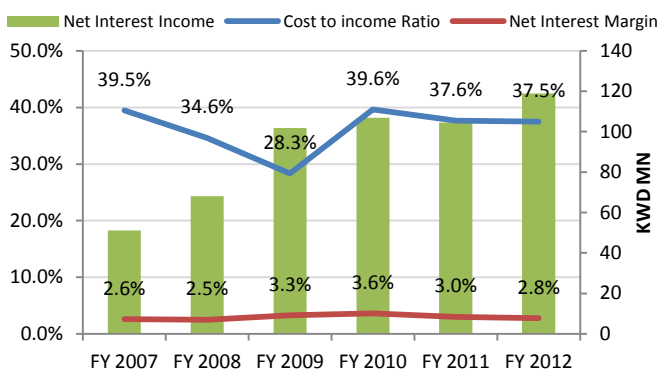
**Trend of NPL's and NPL ratio**

Source: Company financials

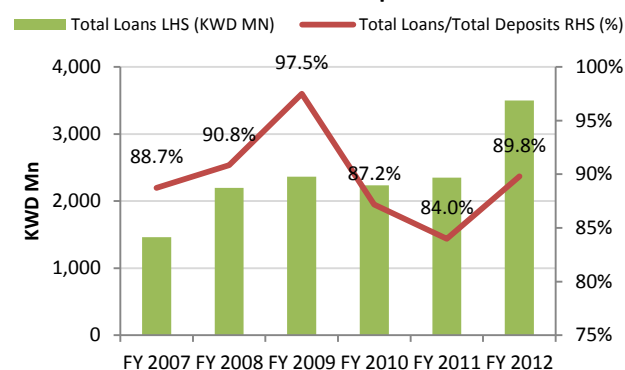
**Trend of provision coverage ratio**

Source: Company financials

- ✦ The group has managed to maintain a stable cost to income ratio despite going in for acquisitions in 2008, 2010 and 2012.

**Margin Analysis**

Source: Company financials

**Loans to deposit ratio**

Source: Company financials

## BURGAN BANK SUBSIDIARIES

### ✦ JORDAN KUWAIT BANK

- ✦ Burgan Bank acquired a 51.1% stake in Jordan Kuwait Bank in 2008 becoming Burgan Bank's largest subsidiary currently accounting for close to 16% of total assets. Jordan Kuwait Bank reported a 7% year-on-year growth in net revenues in 2012 despite the tense political environment in the country. Loans and advances grew 14.5% year-on-year and deposits increased 1.5% year-on-year.

### ✦ BURGAN BANK TURKEY

- ✦ Burgan Bank Turkey (former Eurobank Tefken) is among the top 20 banks in Turkey operating 60 branches spread across 21 major business and industrial cities in Turkey. The bank has grown its network aggressively with branches doubling since 2006. Burgan Bank Turkey has two wholly-owned subsidiaries; Burgan Leasing, engaged in the leasing business having a portfolio size of \$77.2 million (FY 2012) and Burgan Securities, engaged in investment banking activities.

- ✦ Burgan Bank Turkey has seen poor profitability in recent years, underperforming the Turkish banking sector on a number of key metrics. In 2011, Burgan Bank Turkey's cost of funds was close to 8% compared to the industry average of 5.5% while net interest margin worked out to 2.51% as opposed to the sector average of 3.6%. Burgan Bank Turkey should be able to source cheaper funding backed by a foreign parent company which will be a catalyst to growth in the future.
- ✦ **GULF BANK ALGERIA**
- ✦ Gulf Bank Algeria accounts for 6.1% of Burgan Bank Group's total assets and provides conventional as well as Islamic banking services in Algeria through a network of 33 branches. The bank reported a 42.7% year-on-year increase in net profit to KWD 13.7 million on the back of a 52% year-on-year growth in revenues in FY 2012 while customer loans increased 54% year-on-year.
- ✦ **BANK OF BAGHDAD**
- ✦ Bank of Baghdad contributes 4.5% to Burgan Bank's consolidated balance sheet and is one of the largest private commercial banks in Iraq with a presence in Lebanon.
- ✦ **TUNIS INTERNATIONAL BANK**
- ✦ Tunis International Bank contributes 1.7% of Burgan Banks revenues and 2.5% of the Groups assets.
- ✦ **FIMBank, Malta**
- ✦ Burgan Bank has received approval from Kuwait Regulator to acquire 25% stake in FIMbank, Malta. FIMBank shareholders approved the joint offer from United Gulf Bank and Burgan Bank to acquire the 36.56% of FIMbank. FIMBank is a boutique bank offering trade finance products and services across 50 countries.

## FINANCIAL SUMMARY

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FY ended Dec	2010	2011	2012	2013E
<b>PER SHARE INDICATORS</b>				
EPS	0.003	0.032	0.036	0.051
BVPS	0.264	0.288	0.318	0.360
DPS	-	0.009	0.010	0.010

<b>INCOME STATEMENT (KWD '000)</b>				
Net Interest Income	107	105	119	-
Fees and commission	33	38	38	-
Net investment earnings	8	14	20	-
Other operating income	4	5	11	-
Total operating income	165	163	190	245
Loan loss provisions	72	29	36	-
Operating Profit	28	68	79	107
Minority interest	11	7	7	-
Net income	5	51	56	75

<b>BALANCE SHEET (KWD '000)</b>				
<b>ASSETS</b>				
Cash & cash eq	625	567	787	-
Due from Banks	486	843	611	-
Net Loans and advances	2,136	2,252	3,384	-
Net investments	133	149	311	-
Total Assets	4,147	4,552	5,977	-
<b>Liabilities and</b>				
Due to banks and other	811	942	1,025	-
Customer deposits	2,565	2,796	3,895	-
Total liabilities	3,609	3,986	5,357	-
Minority interest	118	118	129	-
Total shareholders'	539	566	620	-

Source: Company disclosure, FINCORP estimates

### RATIO ANALYSIS

FY ended Dec	2010	2011	2012	2013E
<b>VALUATION &amp; PROFITABILITY METRICS</b>				
P/E (x)	153.98	13.46	14.04	11.35
P/BV (x)	1.73	1.50	1.59	1.64
ROE (%)	1.25	11.65	11.85	16.00
ROIC (%)	1.04	3.74	3.59	-
ROA (%)	0.11	1.16	1.06	1.20

### GROWTH ANALYSIS

Loan Growth (%)	(5.43)	5.02	49.00	-
Deposit Growth (%)	5.77	9.00	39.32	-
Assets Growth (%)	1.11	9.75	31.30	-
Net Worth Growth (%)	29.17	6.39	9.72	-
Net Interest Income	12.45	(11.65)	14.06	-
Net Inc Growth (%)	(25.05)	986.19	9.96	-

### MARGIN ANALYSIS

Cost to income ratio (%)	39.62	37.65	37.49	-
Net interest margin (%)	3.62	3.00	2.80	-
Operating Margin (%)	16.70	41.07	40.79	43.6
Net Income Margin (%)	2.80	30.43	28.81	29.9

### KEY METRICS

Capital Adequacy Ratio	15.60	14.70	12.00	-
Loans/Deposits ratio (%)	87.16	83.98	89.81	-
NPL/Gross loans (%)	6.13	11.52	7.07	-
Credit prov/gross loan (%)	3.12	1.27	1.23	-
NPL coverage ratio (%)	1.18	3.95	2.65	-

Source: Company disclosure, FINCORP estimates

## PEER COMPARISON

Name	Mkt Cap (\$MN)	Total Loans (\$MN)	Tot Assets (\$MN)	1Yr Rev Growth	2012 ROE	3Yr Avg ROE	P/E	P/BV
BURGAN BANK	3,345	12,431	21,240	16.1%	11.2%	8.3%	16.92x	1.76x
NATIONAL BANK OF KUWAIT	15,498	36,625	58,369	19.2%	13.2%	13.7%	14.30x	1.84x
GULF BANK	3,865	12,553	17,224	3.8%	7.0%	6.3%	33.83x	2.30x
COMMERCIAL BANK OF KUWAIT	3,112	7,931	13,036	-10.8%	0.2%	3.0%	431.57x	1.61x
KUWAIT INTERNATIONAL BANK	1,124	3,090	4,440	5.8%	6.2%	6.9%	20.95x	1.34x
AHLI UNITED BANK (ALMUTAHED)	3,458	6,420	9,357	1.8%	14.1%	12.8%	22.72x	3.15x
KUWAIT FINANCE HOUSE	8,933	25,146	52,252	7.0%	4.6%	5.1%	27.70x	1.24x
BOUBAYAN BANK K.S.C	4,171	4,625	6,698	23.6%	4.2%	3.7%	111.75x	4.63x
<b>Average</b>	<b>5,438</b>	<b>13,603</b>	<b>22,827</b>	<b>8.3%</b>	<b>7.6%</b>	<b>7.5%</b>	<b>84.97x</b>	<b>2.23x</b>

Note: Price data as on 15-May-13

Source: Company financials, Bloomberg, FINCORP Research

✦ Historically the bank has traded at a cheaper valuation to its peers.

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