

Oman Banking Sector, *rising credit offtake to drive growth* July 25, 2023

| Bank | Rating |
|------------------------------|--------------|
| Bank Muscat (BKMB) | Accumulate |
| Bank Dhofar (BKDB) | Hold |
| National Bank of Oman (NBOB) | Accumulate |
| Bank Sohar (BKSB) | Under Review |
| Ahli Bank (ABOB) | Hold |
| HSBC Oman (HBMO) | Under Review |
| Oman Arab Bank (OAB) | Accumulate |

- Credit growth to pick up to an avg 6% over 2023-27e on improving GDP growth.
- Deposit growth is likely to remain robust on Government's higher oil & gas revenues as Government debt repayments taper off.
- NIMs expected to increase on rising interest rates; Interest rate ceiling of 6% on personal loans to weigh on NIM expansion for retail focused banks.
- In our view, the cost of risk should have peaked in 2022 and we include a tapering off cost of risk over our forecast horizon.

We revisit our target prices and ratings on the Omani Banking sector as follows: Bank Muscat (BKMB) – ACCUMULATE, Bank Dhofar (BKDB) – HOLD, National Bank of Oman (NBOB) – ACCUMULATE, Oman Arab Bank (OAB) – ACCUMULATE, Ahli Bank (ABOB) – HOLD. Sohar International Bank (BKSB) and HSBC Oman (HBMO) continue to be 'Under Review' due to the ongoing merger.

- **Positive oil & gas government revenue to drive credit growth of average 6% over 2023 – 2027e:** Government hydrocarbon revenues will be positively affected under the elevated oil & gas price scenario, further supported by the Government's revenue diversification plans. The IMF forecasts Oman's real GDP to increase by 1.3%YoY in 2023e, followed by further expansionary years, with real GDP output expected to expand by 2.7% in 2024e. Due to Oman banks' heavy reliance on government spending to drive credit growth, we believe credit growth is likely to pick up over 2023-2027e to average 6% over this period.
- **Increasing government spending to provide catalysts for Oman bank stocks:** With the government expenditure to be driven towards Oman Vision 2040 as the general government debt to GDP hits the targeted figure, we see support for increased government spending towards construction and other manufacturing projects driving credit growth giving Oman banking stock prices the necessary impetus going forward.
- **Relative preference in the sector:** Given the higher interest rate environment, we prefer banks that have credit exposure more skewed towards corporates so that a more notable NIM expansion is observed. We note the interest rate ceiling of 6% on personal loans in place in Oman which will weigh on the NIM expansion for retail-focused banks in Oman. We prefer banks with sound capital management policies, better credit supervision, and stronger liquidity profiles.
- **Sector Consolidation:** Oman Banking sector is currently undergoing a consolidation phase with Sohar International Bank merging with HSBC Oman (completion due 17 August 2023). There are ongoing acquisition offers from Bank Dhofar and Oman Arab Bank (via a consortium led by OMINVEST) for a potential acquisition of Ahli Bank.

| Name | Last Px (OMR) | Target Price (OMR) | Upside / (Downside) (%) | Current P/B | P/B'23e (x) | P/E'23e (x) | ROE'23e (%) | Cash Div Yield'23e, %* |
|----------------|---------------|--------------------|-------------------------|-------------|-------------|-------------|-------------|------------------------|
| Bank Muscat | 0.280 | 0.310 | 11% | 1.26 | 1.15 | 9.7 | 12.2% | 5.0% |
| Bank Sohar | 0.105 | UR | - | 0.87 | 0.82 | 10.8 | 7.7% | 2.9% |
| NBO | 0.299 | 0.330 | 10% | 1.02 | 0.98 | 7.6 | 13.2% | 5.9% |
| Bank Dhofar | 0.175 | 0.182 | 4% | 0.94 | 0.90 | 12.5 | 7.3% | 3.2% |
| HSBC Oman | 0.163 | UR | - | 0.92 | 0.88 | 10.5 | 8.5% | 5.6% |
| Ahli Bank | 0.200 | 0.205 | 2% | 1.30 | 1.23 | 11.1 | 11.2% | 4.8% |
| Oman Arab Bank | 0.142 | 0.169 | 19% | 0.65 | 0.62 | 10.4 | 6.2% | 4.3% |
| Average | | | | 0.99 | 0.94 | 10.4 | 9.5% | 4.5% |

Source: Bloomberg, U Capital Research, UR = Under Review

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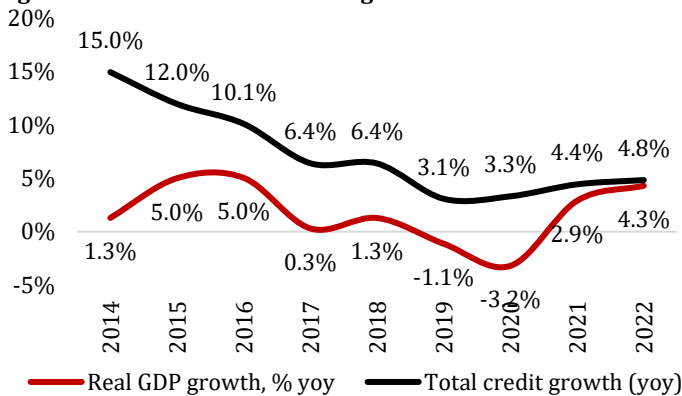
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Macro-economic overview

Oman's economic recovery driven by higher oil prices; moderate growth expected in 2023

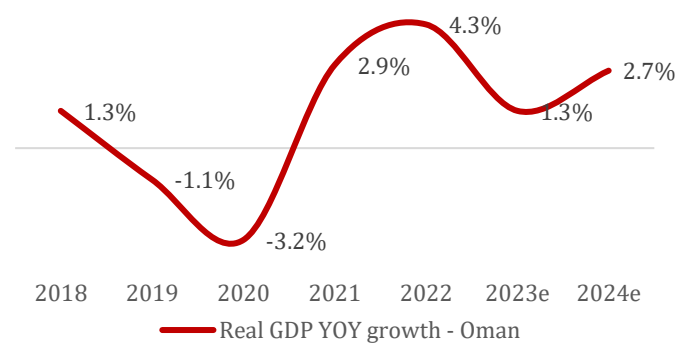
Oman's economic growth in 2021 and 2022, with growth rates of 2.9% and 4.3% in GDP respectively, was driven by the rise in oil prices and supportive fiscal policies implemented by the government, including stimulus packages. Oman's economy is anticipated to continue growing in 2023 albeit at a moderate pace. The moderation reflects the impact of production cuts implemented by OPEC+ on the oil sector. However, the non-oil economy is expected to maintain its growth trajectory, supported by infrastructure projects and a boost to the tourism sector. Various Government-led diversification efforts like Tanfeedh program are expected to drive non-oil revenue and support the Government's coffers for new investments within the country's infrastructure. The IMF expects Oman's economy to grow at a rate of 1.3% in 2023, below the global GDP growth expectations of 2.7%. Oman's economy is estimated to expand further 2.7% in 2024, according to the IMF estimates.

Fig. 1: Oman: Total credit vs GDP growth



Source: CBO, IMF, U Capital Research

Fig. 2: Oman GDP likely to continue its growth trajectory



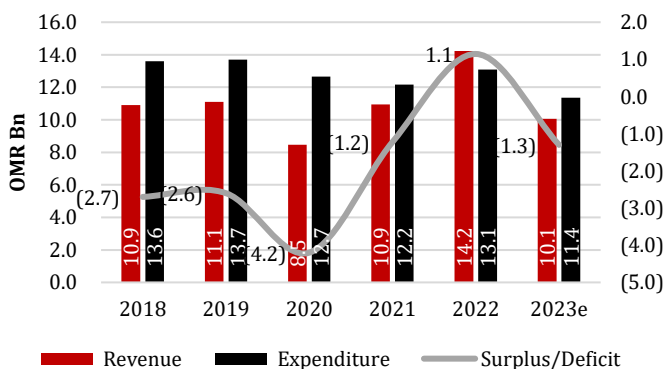
Source: IMF, U Capital Research

The Banks' loan book growth rate correlates quite closely with the changes in the GDP growth rate. As shown in the chart above, the credit growth in the system has directionally followed GDP growth and has exceeded GDP growth by a few percentage points. Looking ahead, we expect an average credit growth of 6% in the system over 2023 – 2027e as GDP growth picks up.

Improving fiscal balance on higher oil prices to support government spending

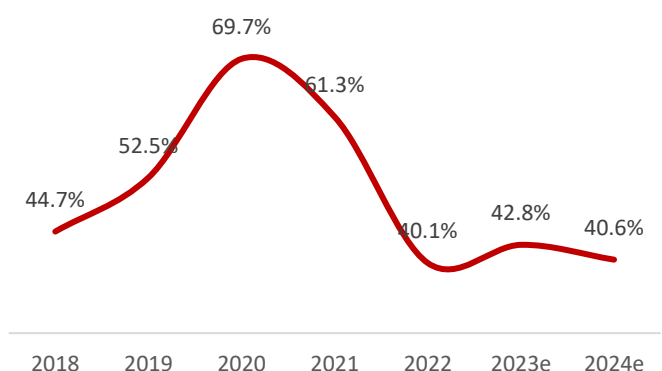
Oman's economy faced challenges leading up to 2021, as it had been grappling with consecutive fiscal deficits for over a decade. However, in 2022, the country experienced a significant turning point as it achieved a fiscal surplus for the first time in approximately 10 years driven by a strong recovery in oil prices. Crude oil prices have recently declined from their peak and are currently trading within the range of USD 72-78 per barrel driven by slowdown in the global economy.

Fig. 3: Oman fiscal budget



Source: Ministry of Finance Oman, U Capital Research

Fig. 4: General govt. gross debt as % of Oman GDP



Source: IMF, U Capital Research

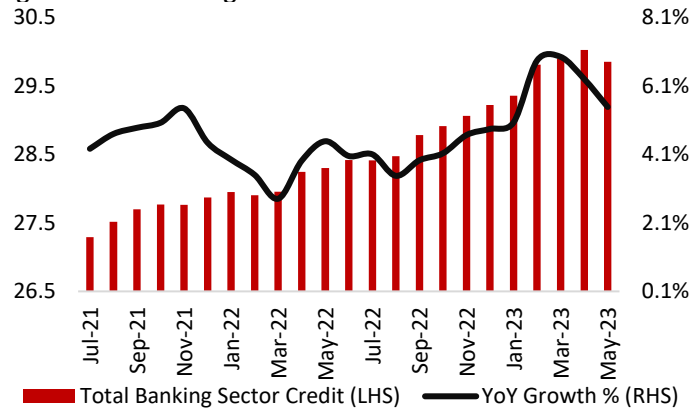
Higher fiscal revenue resulting from the improved oil prices is leading to a decline in general government gross debt as a percentage of GDP. Once the general government gross debt as a % of GDP hits the targeted figure, the government will have further room to raise spending across sectors, with a particular focus on non-oil industries. Overall, the positive development in oil prices, the improved fiscal balance, and the anticipated decline in government debt as a percentage of GDP provide a favorable environment for increased government spending across sectors. Consequently, the demand for business and household lending along with an overall improvement in credit conditions appears to remain supportive of economic growth.

Oman Banking Landscape

The banks rely on government spending to drive credit growth and at the same time banks include a large proportion of government and public sector deposits in the system (at c.33% at end-April 23). As a result, banks in Oman have considerably high exposure to sovereign credit risk through sizeable holdings of sovereign/central bank assets. The total credit and deposit growth in Omani banks has been quite robust over the last couple of years as shown in the chart below, showing steady growth.

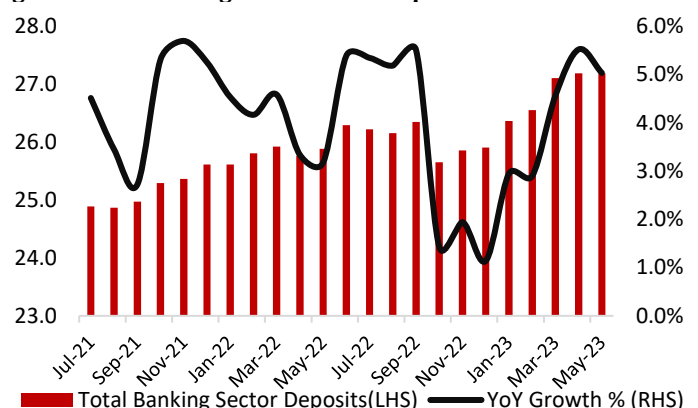
Oman's Vision 2040 is further supportive of banks growth as they stand to benefit from an expected expansionary fiscal policy. Opportunities for the banks to finance government-related projects will likely improve and we expect overall sector credit growth to pick up to an average of 6% over 2023-2027e.

Fig. 5: Omani Banking Sector: Total Credit



Source: CBO, U Capital Research

Fig. 6: Omani Banking Sector: Total Deposits

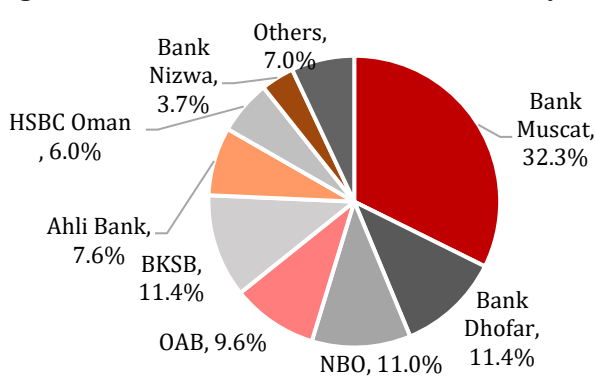


Source: CBO, U Capital Research

Market share of Oman banks

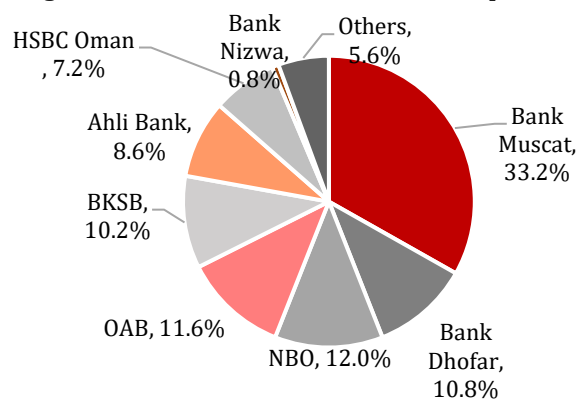
The Omani Banking sector consists of 7 local, 2 specialized, 9 commercial and 2 full-fledged Islamic Banks. The local Banks have separate Islamic Banking subsidiaries as well. Conventional Banking in Oman is predominantly managed by the 7 listed banks. For the unversed, Bank Muscat is the largest bank in Oman with 32.3% market share of assets and 33.2% market share in terms of total deposits. Bank Muscat is followed by Bank Dhofar which has a market share of 11.4% of the total assets. Post completion of Bank Sohar and HSBC merger, the combined entity will be the second largest entity among Omani banks.

Fig. 7: Omani Banks: Market share, total assets May 2023



Source: CBO, U Capital Research

Fig. 8: Oman Banks market share - total deposits, May 2023

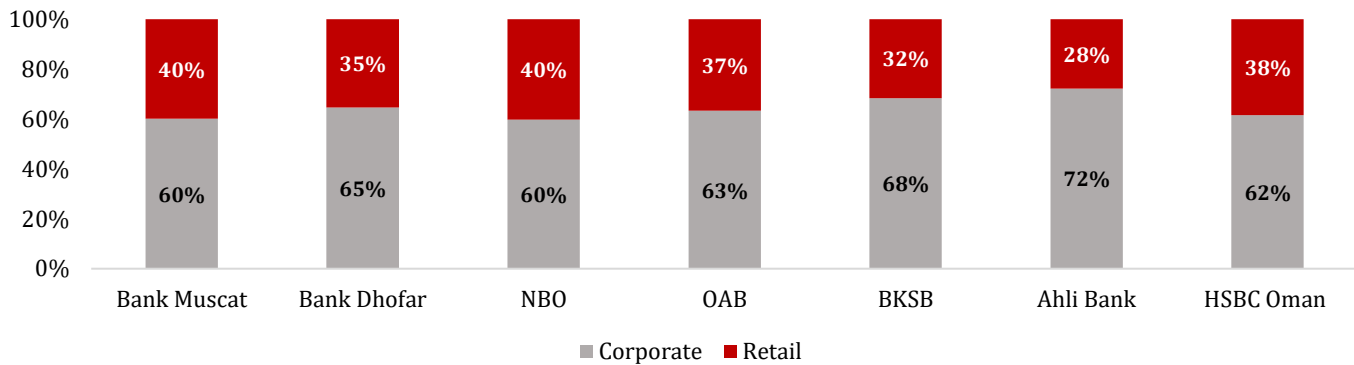


Source: CBO, U Capital Research

Credit concentration

As of 1Q23, Ahli Bank (ABOB) had the highest exposure (at 72% of its total gross credit portfolio) to the corporate & commercial sector among the listed conventional banks in Oman, closely followed by Bank Sohar at 68% exposure to corporate sector.

Fig. 9 : Omani Banks: Credit Concentration 1Q23



Source: Banks financials, U Capital Research

Within its corporate & commercial exposure, ABOB has the highest exposure to construction, wholesale and retail trade and financial institutions. ABOB is followed by Bank Sohar, whose Corporate & commercial exposure is more skewed towards the construction and manufacturing sectors.

Fig. 10: Omani Banking Sector: Heat map for economic sector exposure, FY 2022

| Heat map for economic sector exposure | BKMB | BKDB | NBOB | OAB | BKSB | ABOB | HBMO | BKNZ | Sector FY22 |
|---|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|
| Personal and consumer loans/housing loans | 42% | 37% | 41% | 34% | 30% | 30% | 37% | 39% | 38% |
| Corporate and commercial | 58% | 63% | 59% | 66% | 70% | 70% | 63% | 61% | 62% |
| Import trade | 5% | 3% | 2% | 3% | 0% | 0% | 9% | 0% | 4% |
| Construction | 5% | 11% | 4% | 8% | 14% | 16% | 7% | 8% | 8% |
| Export Trade | 1% | 0.2% | 0.0% | 0.0% | 0.1% | 0.0% | 0.0% | 0% | 0.2% |
| Manufacturing | 8% | 5% | 5% | 8% | 12% | 9% | 10% | 9% | 8% |
| Wholesale and retail trade | 2% | 3% | 4% | 4% | 10% | 8% | 2% | 0% | 4% |
| Electricity, gas, water | 8% | 5% | 6% | 4% | 4% | 3% | 4% | 0% | 7% |
| Transportation and communication | 9% | 3% | 7% | 7% | 4% | 8% | 0% | 0% | 6% |
| Services | 8% | 11% | 10% | 11% | 16% | 13% | 5% | 25% | 8% |
| Mining and quarrying | 3% | 3% | 4% | 5% | 6% | 0% | 2% | 0% | 4% |
| Others | 1% | 9% | 2% | 10% | 0% | 3% | 24% | 19% | 3% |
| Financial Institutions | 4% | 6% | 7% | 5% | 3% | 7% | 0% | 0% | 5% |
| Real Estate | 3% | 0% | 0% | 0% | 0% | 0% | 0% | 0% | 0% |
| Government | 0% | 4% | 7% | 0% | 0% | 3% | 0% | 0% | 4% |
| Agriculture & Allied Activity | 2% | 0% | 0% | 1% | 0% | 0% | 0% | 0% | 0% |
| Non-resident | 0% | 0% | 1% | 0% | 0% | 0% | 0% | 0% | 1% |
| Total | 100% | 100% | 100% | 100% | 100% | 100% | 100% | 100% | 100% |

Source: Bank Financials, 2022 and CBO

*Sector is Conventional Banks only, ex-Islamic Financing; All banks include Islamic Finance, if applicable; Data as at the end of 2022

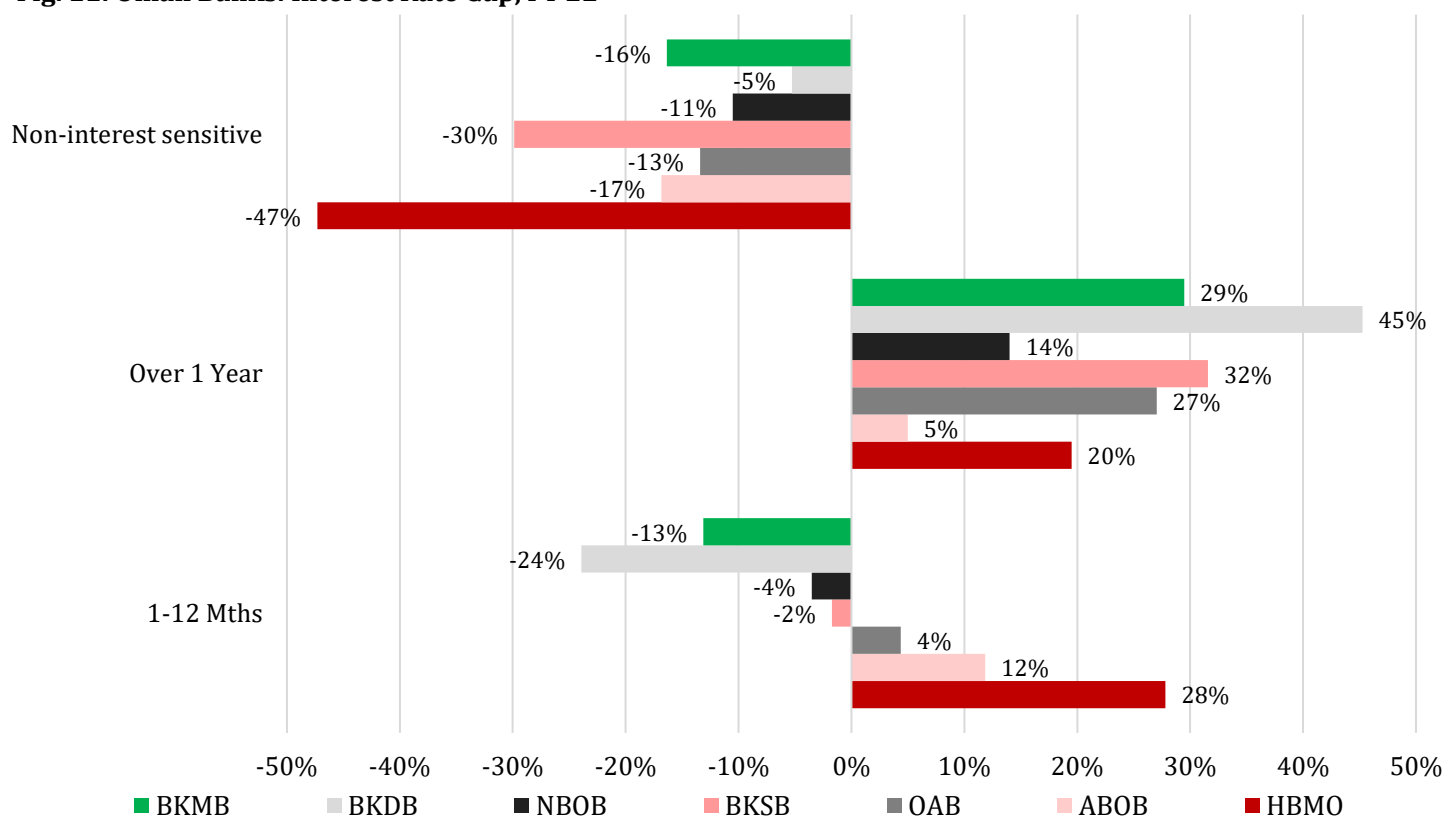
The banking sector in Oman is exposed to the real estate market with a total direct and indirect real estate exposure of over one-third of their lending portfolio. Within this real estate exposure, residential mortgages formed around 17.5% of lending in 2022. In addition, commercial real estate exposure formed around 3.4% of the total lending portfolio.

Despite a backdrop of rising interest rates, long maturity profiles, the prevalence of fixed-rate mortgages, and stabilization of property prices and support from improvement in economic and demographic indicators relieve any immediate concerns regarding residential. Although vulnerabilities may reemerge, any decline in real estate valuations is unlikely to spur strategic defaults due to adequate margins (at least 20%) and the prevalence of recourse debts.

Positive interest rate gap for 2024 and beyond

Beyond 2023, all seven listed conventional banks' interest rate gap is positive, indicating that as interest rates increase, the bank's assets are repriced at higher rates. In this scenario, net interest income for 2024 and beyond is expected to increase for most banks, whilst performing loans are preserved.

Fig. 11: Oman Banks: Interest Rate Gap, FY 22



Source: Bank Financials for 2022, U Capital Research

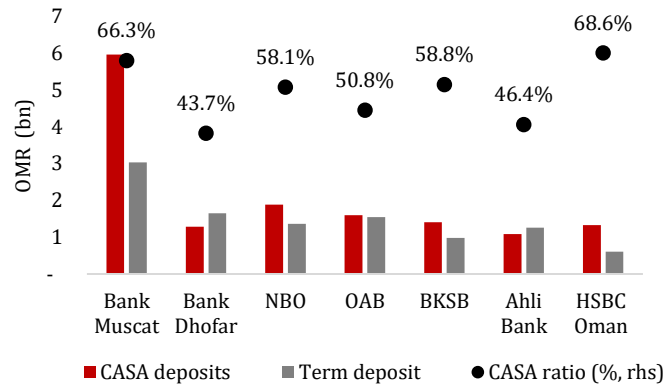
Interest rate gap calculated as assets minus liabilities for each maturity time bracket as % of total assets.

Amongst banks, Bank Dhofar (BKDB), Sohar International Bank (BKSB), Bank Muscat (BKMB) and Oman Arab Bank (OAB) have the largest positive interest rate gap over 1 year. It is worthwhile to note that all banks also have a negative gap in non-interest sensitive assets, indicating support to interest income from non-interest sensitive liabilities in times of rising interest rates, as cost of funding is supported by such liabilities. HBMO and BKSB sport large chunks of their assets funded by non-interest sensitive liabilities. Banks with higher funding from non-interest-bearing liabilities are expected to fare better than the others in terms of improvement in net interest margin.

Omani Banks deposit mix: Healthy CASA deposit ratios

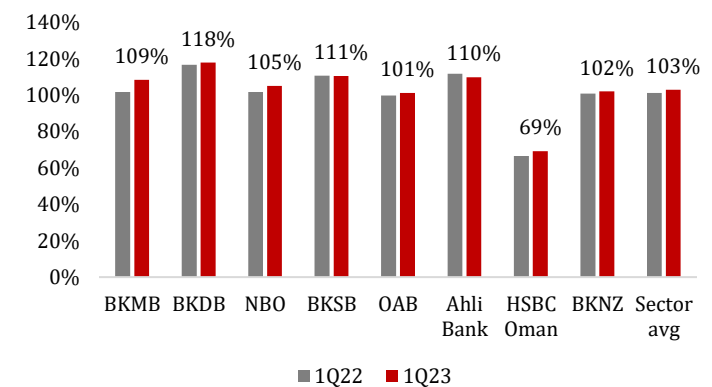
In times of rising interest rates, a higher reliance on low-cost deposits helps to grow interest income through a low cost of funding. HSBC Oman has the largest CASA Ratio at 68.6%, as of 1Q23 whereas BKDB has the lowest at about 43.7%. In fact, for all banks except Bank Dhofar and Ahli Bank, CASA Ratio is more than 50%.

Fig. 12: Omani Banking Sector: Total Credit, 1Q23



Source: Banks financials, U Capital Research

Fig. 13: Omani Banking Sector: Loans to deposit ratio, 1Q23



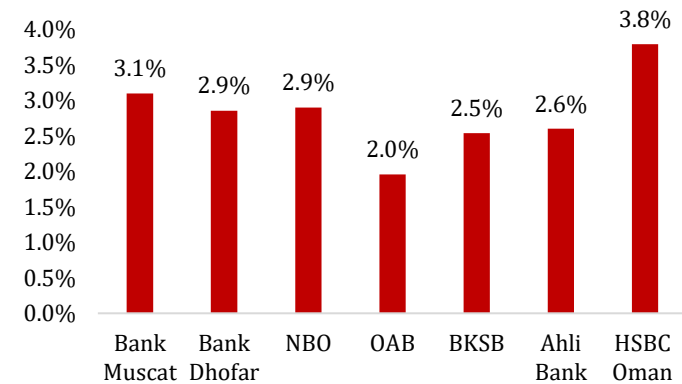
Source: Banks financials, U Capital Research

The loan to deposit ratio for most banks is in the range of 101% - 111%; clear exception on the higher side being Bank Dhofar with a loan to deposit ratio of 118% and on the lower side is HSBC Oman, with a loan to deposit ratio of 69%.

Banks with high corporate exposure should see further NIMs expansion

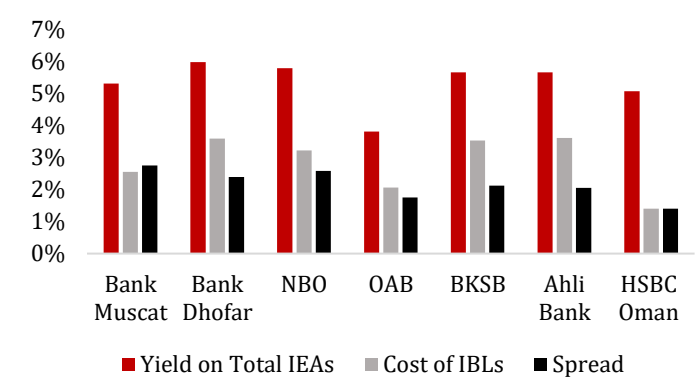
The yield on average assets has been in a stable range across banks at 3.81% to 5.98%. BKMB's average NIMs was reported at around 3.1% in 1Q23, this is on account of the large asset base. The highest NIMs across the sector were reported by HSBC Oman.

Fig. 14: Omani Banks: Net Interest Margins, 1Q23



Source: Banks financials, U Capital Research

Fig. 15: Omani Banks: Spreads, 1Q23



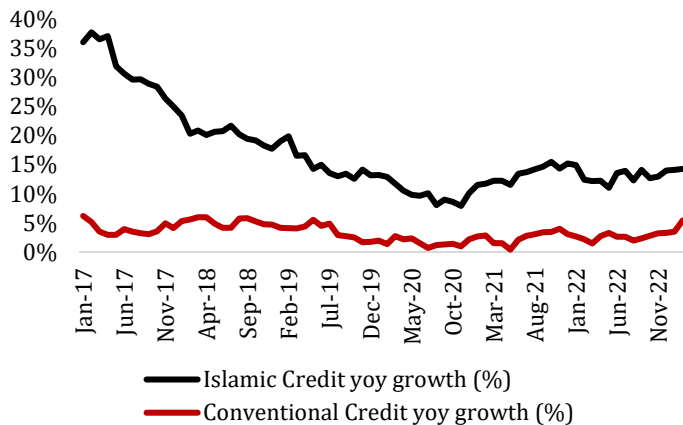
Source: Banks financials, U Capital Research

Among the Banks, Bank Dhofar has the highest yield on assets at 5.98% in 1Q23, followed by NBO, which has seen its yield on assets at 5.5%. NBO's has a 44% share of personal loans due to its high exposure to the retail clients, this has been attributed to a higher yield on assets for the Bank. However, considering the higher low-cost deposit base (CASA ratio), we see the spread highest for Bank Muscat. We expect NIM expansion for Ahli Bank going forward, owing to their higher corporate loan exposure.

Islamic Banking: a significant growth driver

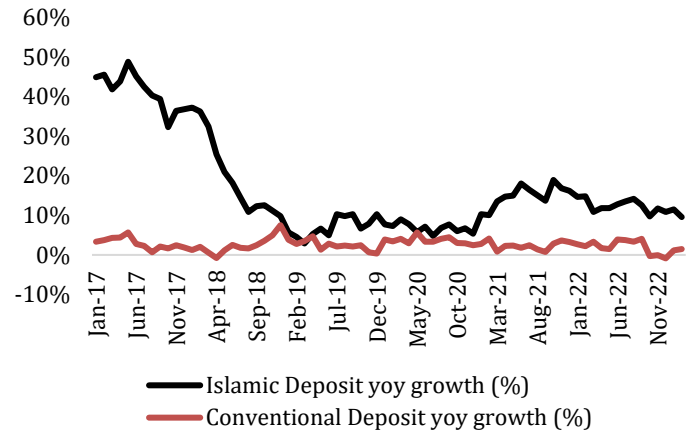
Islamic banking has seen significant growth in deposits and loans in the Oman Banking landscape. The growth rates for Islamic Banking have been significantly higher than conventional banking. For instance, BKMB's Islamic assets have grown from OMR1.16bn to OMR1.45bn from 2018 to 2022, translating to a CAGR of 6.9%, compared to 0.4% growth in conventional loans.

Fig. 16: Oman Islamic vs Conventional Credit Growth



Source: CBO, U Capital Research

Fig. 17: Oman Islamic vs Conventional Deposit Growth



Source: CBO, U Capital Research

We note the increasing focus of Oman Banks towards Islamic Banking and show the number of branches each bank has for their conventional business and Islamic windows. Bank Muscat has the highest number of branches for its Islamic window, Meethaq. This is followed by Ahli Bank with 19 offices for Al Hilal, its Islamic window. This is equal to Bank Nizwa, a purely Islamic bank.

Fig. 18: Number of Branches of Oman Banks and their Islamic Windows

| | Date of Establishment | Authorised Offices | Operating Offices |
|------------------------------------|-----------------------|--------------------|-------------------|
| Local Banks | | | |
| NBO | 1973 | 59 | 59 |
| OAB | 1973 | 47 | 47 |
| HBMO | 1975 | 46 | 46 |
| BKMB | 1981 | 145 | 145 |
| BKDB | 1990 | 60 | 60 |
| BKSB | 2007 | 30 | 30 |
| ABOB | 1997 | 24 | 24 |
| Total | | 411 | 411 |
| Islamic Banks & Windows | | | |
| Bank Nizwa | 2012 | 19 | 19 |
| Alizz Islamic Bank | 2013 | 16 | 16 |
| BKMB-Meethaq NBOB-Muzn | 2013 | 24 | 24 |
| NBO- Muzn | 2013 | 6 | 6 |
| BKDB-Maisara | 2013 | 10 | 10 |
| ABOB-Al Hilal | 2013 | 19 | 19 |
| BKSB-Sohar Islamic | 2013 | 8 | 8 |
| Total | | 102 | 102 |

Source: CBO, Quarterly Statistical Bulletin March 2023

Most banks across Oman have observed increasing contribution from their Islamic windows. Bank Muscat's Meethaq asset base has grown from OMR1.16bn to OMR1.45bn from 2018 to 2022, translating to a CAGR of 6.9%, compared to 0.4% growth in conventional loans.

A look at asset quality metrics

Oman banks' stage-wise Expected Credit Losses (ECL) data indicates that over 70% of each bank's exposure is in Stage 1 of impairment or in simpler words, is performing, with the remainder being in Stage 2 and Stage 3, except for HSBC Oman, which is at 59%. Within Stage 3 exposure, only HBMO and BKMB have provided for over 80% of the exposure, while all others have provided for over 60% of exposure, except Bank Dhofar and Sohar International Bank. The highest exposure in Stage 3 (NPLs) is for Bank Dhofar (7%) and Oman Arab Bank (at about 6%), while the lowest exposure in Stage 3 is for Bank Muscat, HSBC Oman and Ahli Bank.

Fig.19: Oman Banks: Stages of impairment of exposure as % Total Loans -1Q23

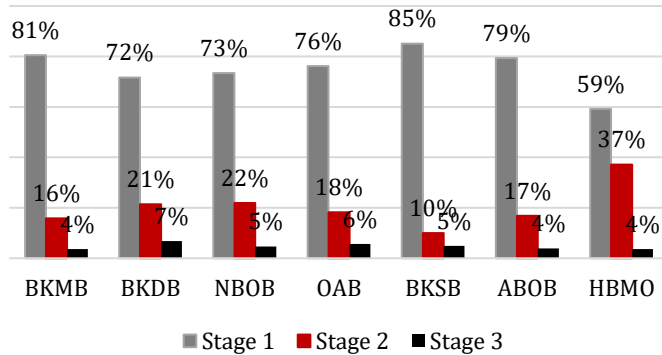
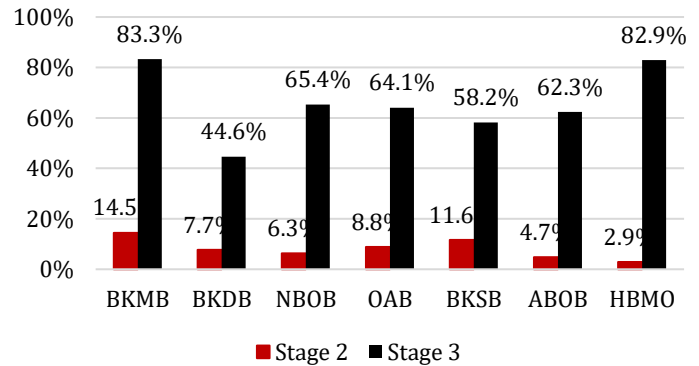


Fig. 20: Oman Banks: Stage 2 & Stage 3 ECL Provision as % of Exposure -1Q23



* Oman Banks: Stages of impairment of exposure as % of Total Loans (Including Islamic financing where applicable) -1Q23

Source: Bank Financials, U Capital Research

Bank Muscat and HSBC Oman have provision cover > 100%, indicating prudent provisioning norms. NBO and OAB are close to 100% provision coverage. Sohar International and Ahli Bank are close to 91% coverage each. On the other end, Bank Dhofar has the lowest provision coverage among Omani Banks which stands at 73%. HSBC Oman has the lowest NPL ratio at 1.8%.

Fig.21: Oman Banks: Total Provision as % of Total Loans & Islamic Financing - 1Q23

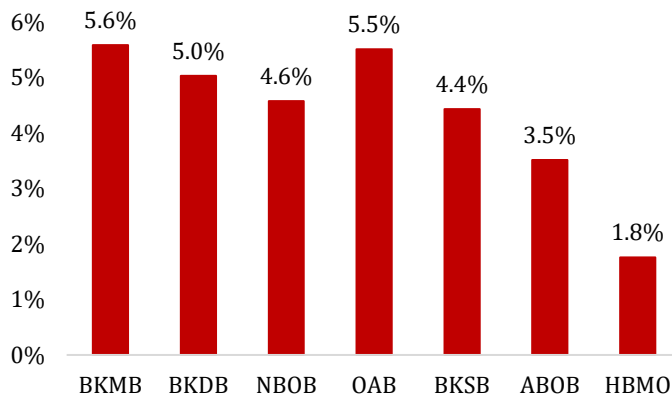
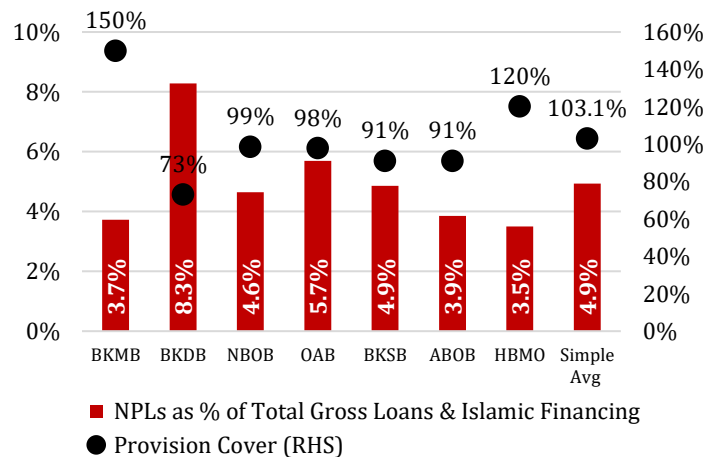


Fig.22: Oman Banks: Asset Quality -1Q23



Source: Bank Financials, U Capital Research

Ahli Bank, Bank Dhofar and OAB have the highest percentage of restructured loans; however, for Ahli Bank and Oman Arab Bank more than 50% of restructured loans are classified as Stage 3 or non-performing.

Fig.23: Oman Banks: Restructured Loans as % of Total Loans & Islamic Financing

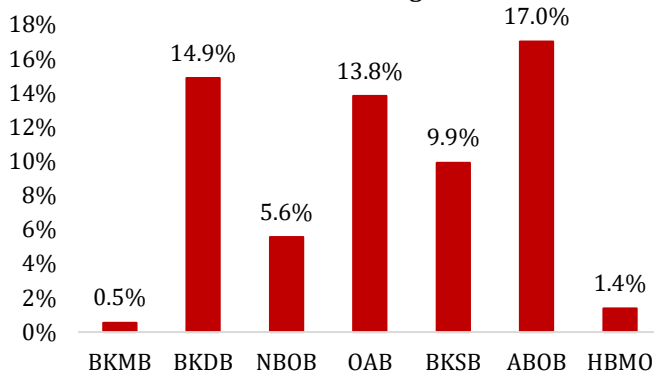
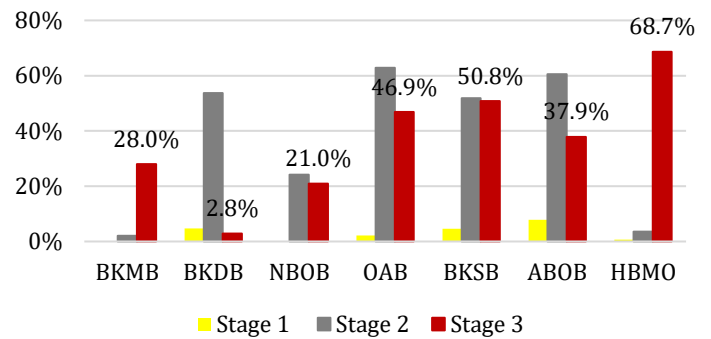


Fig.24: Oman Banks: Stage-wise Restructured Loans as % of Total Loans & Islamic Financing



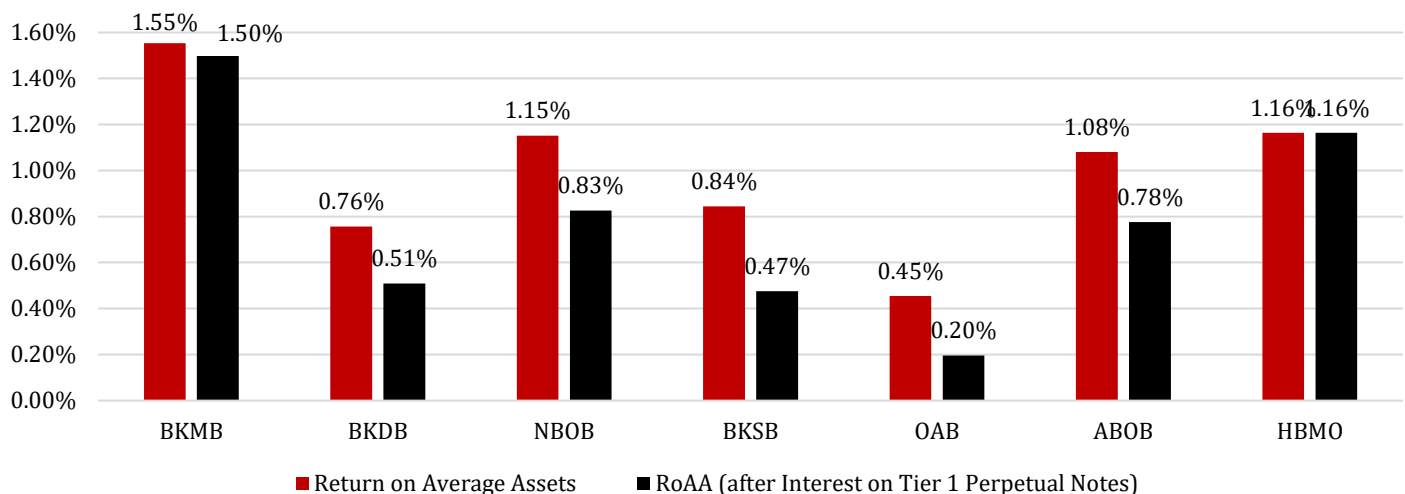
Source: Bank Financials, U Capital Research

Overall, NPL ratio (non-performing loans & Islamic financing to gross loans & Islamic financing) is low for the sector (as compared to some of its GCC counterparts), although it has climbed up over the last few years. We believe that we might not see any significant pressure on NPLs due to the ongoing economic recovery in the country.

Banks profitability ratios briefly

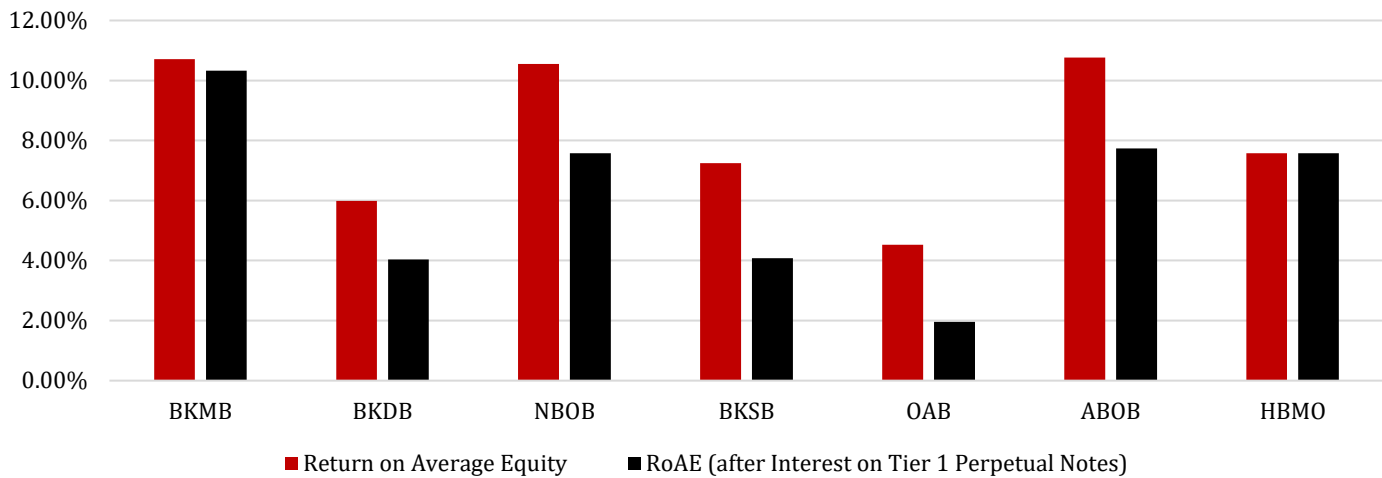
A rush to preserve capital adequacy ratios whilst remaining competitive in loan growth has led many banks to raise Tier 1 Perpetual Notes as customer deposit growth remained muted in the past few years. While expected to boost income in the longer run through growth in loans, the interest payment on these instruments has negatively affected the profitability ratios of most banks.

Fig. 25: Oman Banks: Return on Average Assets, 2022



It must be noted this interest is paid through equity directly and does not affect income through cost of funding. However, recently, many banks have chosen to redeem some of their existing Tier 1 Perpetual securities, and either issue new ones in their place with lower interest rates or issue none. HSBC Oman has never issued any Tier 1 capital as its Core Equity Tier 1 (CET1) ratio is very high.

Fig. 26: Oman Banks: Return on Average Shareholders' Equity, 2022

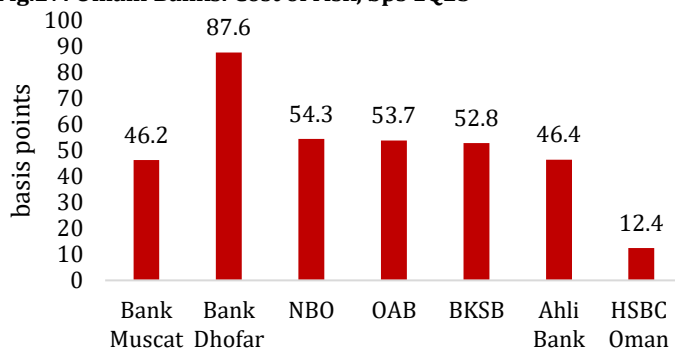


Source: Bank Financials, U Capital

Cost to income ratio and cost of risk vary across the sector

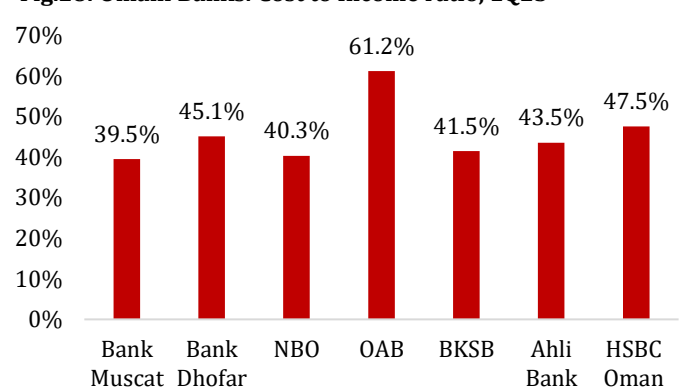
Oman Banks are focusing on virtual banking by investing in technology and digitizing their operations as well as opening more physical branches. Among Oman banks, Bank Muscat has the lowest cost to income ratio at 39.5%, followed by NBO with cost to income at 40.3% as of 1Q23. OAB has the highest cost to income ratio of 61.2% in 1Q23; OAB has had a historically high cost to income ratio, which had seen a dip in FY19, however post-acquisition the combined costs once again moved higher.

Fig.27: Omani Banks: Cost of risk, bps 1Q23



Source: Banks financials, U Capital Research

Fig.28: Omani Banks: Cost to Income ratio, 1Q23



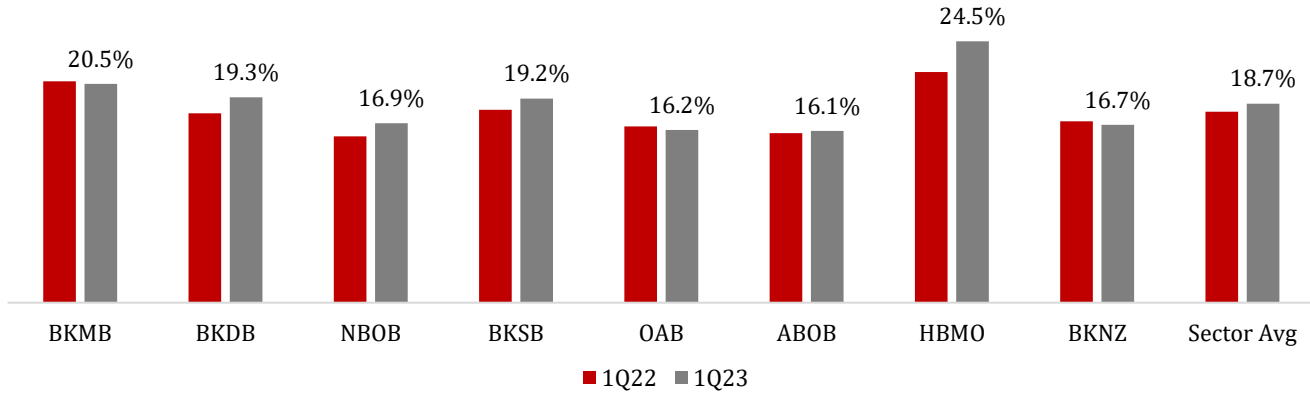
Source: Banks financials, U Capital Research

For 2Q23, from the initially un-audited results reported by banks, Bank Muscat has reported an improvement in cost to income ratio at 38.1%. Oman Arab Bank also reported an improvement in the cost to income ratio for 2Q23 at 56.4%

Oman banks boast robust capital adequacy

Oman banks boast ample capital adequacy levels as at end-1Q23. Within banks, Ahli Bank has the lowest capital adequacy ratio (CAR) at 16.1% at end-1Q23. However, it is still well above the regulatory minimum prescribed by the Central Bank of Oman (CBO).

Fig.29: Oman Banks: Capital Adequacy Ratio (CAR)



Source: Bank Financials, U Capital Research, Sector Avg is simple average.

Note: CBO requires the registered banks in the Sultanate of Oman to maintain minimum capital adequacy of 12%. Additionally, the CAR threshold requires a capital conservation buffer (CCB) of 2.5% annually in addition to 1% of prompt corrective action. On 18 March 2020, CBO relaxed the CCB requirements to 1.25% and accordingly the minimum capital adequacy requirement has been reduced respectively.

Within banks, BKSB has significantly boosted its CET1 Ratio through rights issue (in 2022) which boosted its capital by 50% ahead of its merger with HSBC Oman. ABOB and Oman Arab Bank are on the lower end of the spectrum for CET 1 but continue to remain comfortably above the regulatory minimum of 8.25%. Tier 1 capital ratio of all banks is strong with issuance of Tier 1 perpetual securities by all banks except HBMO (regulatory minimum at 10.25%).

Fig.30: Oman Banks: Common Equity Tier 1 (CET1) Ratio

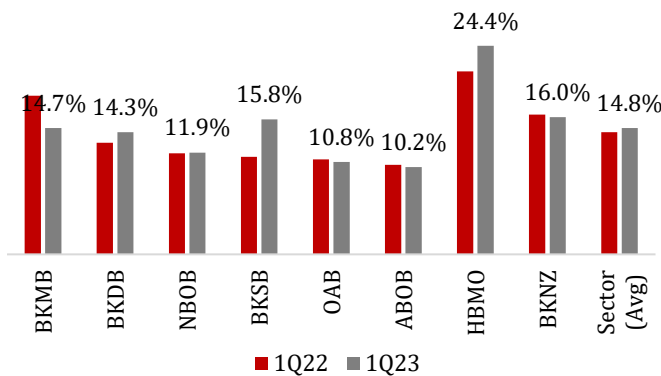
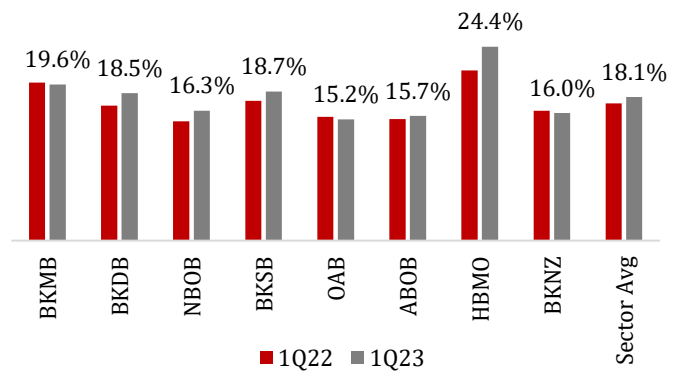


Fig.31: Oman Banks: Tier 1 Capital Ratio



Source: Bank Financials, U Capital Research, Sector Avg is simple average.

Consolidation: ongoing in the Oman Banking sector

Oman Banking sector is currently undergoing consolidation with the merger between Sohar International Bank and HSBC Oman to be completed by end-2023. The merger has received approvals from relevant regulatory bodies as well as from the respective shareholders of the two banks and is on track for completion in the second half of 2023. Currently, a consortium led by OMINVEST and Bank Dhofar have both made acquisition bids for Ahli Bank which is being considered by shareholders and a final decision is yet to be announced. **We believe that consolidation efforts will continue and are necessary in an over-banked market like Oman.**

Peer Group Comparison

| Name | Mkt Cap (OMR mn) | Last Px (OMR) | Px Change (YTD), % | P/B'23e, (x) | P/E'23e, (x) | ROE'23 e, % | Div Yield'23e, % |
|----------------------------|---------------------|------------------|-----------------------|-----------------|-----------------|----------------|---------------------|
| FIRST ABU DHABI BANK PJSC | 16,490.0 | 1.493 | -17% | 1.3 | 11.6 | 12% | 4.1% |
| QATAR NATIONAL BANK | 15,572.5 | 1.686 | -11% | 1.5 | 9.8 | 16% | 4.3% |
| EMIRATES NBD PJSC | 10,825.3 | 1.714 | 26% | 1.0 | 6.4 | 17% | 4.5% |
| RIYAD BANK | 10,531.4 | 3.510 | 8% | 1.8 | 12.2 | 16% | 4.0% |
| NATIONAL BANK OF KUWAIT | 9,615.6 | 1.213 | -6% | 1.9 | 14.3 | 14% | 3.9% |
| SAUDI BRITISH BANK | 8,468.2 | 4.121 | 3% | 1.3 | 11.4 | 13% | 4.8% |
| ABU DHABI COMMERCIAL BANK | 6,698.3 | 0.915 | 2% | 1.0 | 9.2 | 11% | 5.4% |
| BANQUE SAUDI FRANSI | 5,450.0 | 4.522 | 8% | 1.4 | 11.8 | 12% | 4.7% |
| BANK ALBILAD | 4,619.0 | 4.619 | 1% | 2.7 | 18.1 | 16% | 1.5% |
| ARAB NATIONAL BANK | 4,334.2 | 2.889 | -12% | 1.2 | 10.9 | 11% | 5.1% |
| ABU DHABI ISLAMIC BANK | 4,279.1 | 1.178 | 23% | 2.0 | 10.4 | 21% | 5.2% |
| COMMERCIAL BANK PQSC | 2,565.3 | 0.634 | 20% | 1.1 | 8.8 | 14% | 4.9% |
| MASRAF AL RAYAN | 2,443.3 | 0.263 | -22% | 1.0 | 15.3 | 7% | 5.0% |
| BANKMUSCAT SAOG | 2,101.8 | 0.280 | 2% | 1.1 | 9.7 | 12% | 5.0% |
| SAUDI INVESTMENT BANK/THE | 1,790.1 | 1.790 | 1% | 1.2 | 9.7 | 7% | 4.4% |
| COMMERCIAL BANK OF KUWAIT | 1,291.6 | 0.702 | 12% | | 13.4 | 12% | 3.6% |
| DOHA BANK QPSC | 548.0 | 0.177 | -14% | 0.5 | 7.4 | 7% | 6.7% |
| BANK DHOFAR SAOG | 524.4 | 0.175 | 0% | 0.9 | 12.5 | 7% | 3.2% |
| NATIONAL BANK OF OMAN SAOG | 486.2 | 0.299 | 3% | 1.0 | 7.6 | 13% | 5.9% |
| SOHAR INTERNATIONAL BANK | 482.0 | 0.105 | -1% | 0.8 | 10.8 | 8% | 2.9% |
| AHLI BANK | 389.9 | 0.200 | 17% | 1.2 | 11.1 | 11% | 4.8% |
| HSBC BANK OMAN | 326.1 | 0.163 | -2% | 0.9 | 10.5 | 8% | 5.6% |
| OMAN ARAB BANK SAOG | 237.1 | 0.142 | 4% | 0.6 | 10.4 | 6% | 2.9% |
| BANK NIZWA | 212.5 | 0.095 | -5% | 0.8 | 11.8 | 7% | 4.3% |
| Average | | | | 1.2 | 11.0 | 12% | 4.4% |
| Median | | | | 1.1 | 10.8 | 12% | 4.6% |

Source: U Capital Research, Bloomberg

Sorted by market cap.

Fig. 32: Price to Earnings & Dividend Yield

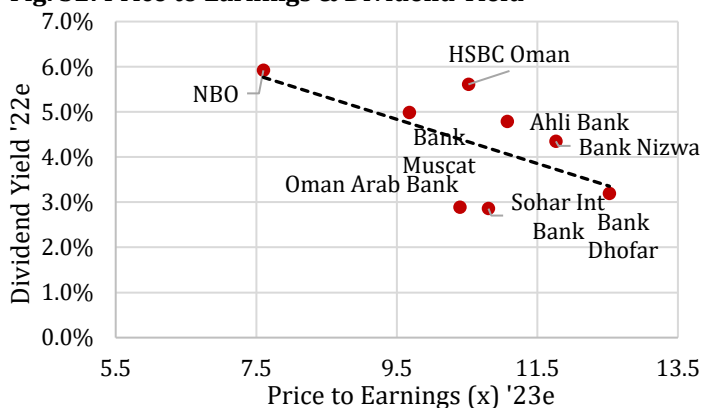
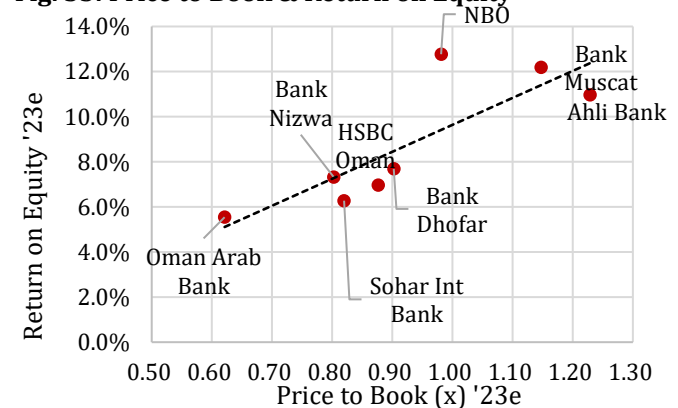


Fig. 33: Price to Book & Return on Equity



Source: Bloomberg, U Capital Research, 1Q23 Financials

Valuation

Our target price is based on blended valuation methodologies – (i) Excess Return methodology (90% weightage) and (ii) Relative Valuation (10% weightage, using P/BV 2023e multiples). We have used a risk-free rate of 6.0%, equity risk premium of 4.8%, and a 5-yr weekly adjusted Beta for individual stocks (Source: Bloomberg). Our base case cost of risk assumption for the year 2023e is based on each bank's performance profile, while P/B ratio sector average assumption is 0.92x for 2023e. For Bank Muscat we assign a 15% premium to this peer average to get a fair value based on relative valuation.

We have assumed a terminal growth rate in the range of 4-5% for each bank based on retention ratio and terminal ROE assumption. Our target prices are based on cost of equity derived from Oman's 10Yr International bond's average mid-yield to maturity and country risk premium. We have assumed spreads to improve given the ample system liquidity and rising interest rates. Any deterioration on the contrary is likely to provide a downside to our valuations.

Summary table of our valuation assumptions across the coverage is shown below:

Fig. 34: Summary valuation Omani Banks

| | BKMB | BKSB | NBOB | BKDB | HBMO | ABOB | OAB |
|--|-------------------|-----------|-------------------|--------------|-----------|--------------|-------------------|
| Excess Returns Method | | | | | | | |
| Current Equity Invested, OMR mn | 1,668 | - | 477 | 553 | - | 312 | 356 |
| PV of Excess Returns & Terminal Value | | | | | | | |
| Year 1 | 23 | - | 8 | -22 | - | 4 | -9 |
| Year 2 | 20 | - | 15 | -18 | - | 5 | -5 |
| Year 3 | 16 | - | 21 | -12 | - | 5 | 0 |
| Year 4 | 15 | - | 24 | -2 | - | 5 | 4 |
| Year 5 | 14 | - | 28 | 0 | - | 5 | 8 |
| Terminal | 631 | - | -34 | 47 | - | 75 | -81 |
| Assumptions | | | | | | | |
| Risk Free Rate | 6.0% | 6.0% | 6.0% | 6.0% | 6.0% | 6.0% | 6.0% |
| Risk Premium (Market Risk, Company Risk, Beta) | 4.8% | 4.8% | 4.8% | 4.8% | 4.8% | 4.8% | 4.8% |
| Cost of Equity (COE) in extraordinary growth | 11.2% | 12.2% | 11.7% | 11.6% | 11.2% | 9.9% | 8.9% |
| Terminal Growth Rate | 5% | 5% | 4% | 5% | 5% | 4% | 5% |
| Fair Value of Equity | 2,387 | - | 539 | 546 | - | 411 | 274 |
| Outstanding Share (mn) | 7,506 | 4,554 | 1,626 | 2,996 | 2,000 | 1,950 | 1,669 |
| Fair Value, OMR | 0.318 | - | 0.332 | 0.182 | - | 0.211 | 0.164 |
| Multiples Method | | | | | | | |
| BVPS'23e | 0.244 | - | 0.305 | 0.194 | - | 0.163 | 0.229 |
| Peer-group P/B'23e | 1.1 | - | 0.9 | 0.9 | - | 0.9 | 0.9 |
| Fair Value, OMR | 0.267 | - | 0.280 | 0.178 | - | 0.150 | 0.216 |
| Weighted Average Fair Value (OMR) | | | | | | | |
| | 0.310 | UR | 0.330 | 0.182 | UR | 0.205 | 0.169 |
| Current Market Price (OMR) | 0.280 | 0.103 | 0.299 | 0.175 | 0.155 | 0.200 | 0.149 |
| Upside/(Downside) | 11% | - | 10% | 4% | - | 2% | 13% |
| Recommendation | Accumulate | UR | Accumulate | Hold | UR | Hold | Accumulate |

UR = Under Review

Source: Bloomberg, U Capital Research, 1Q23 Financials

Risks

Key downside risks:

- Deterioration in macroeconomic indicators warranting a rise in cost of equity.
- Deterioration in hydrocarbon prices, negatively affecting the country's fiscal spending which could also lead to a slower-than-expected credit offtake.
- Event risks as concentrations exist both on assets as well as deposits side.
- Deterioration in asset quality and loan-loss coverage levels resulting in higher-than-expected cost of risk.

Key upside risks to our valuation include:

- Further improvement in sovereign risk profile resulting in a lower cost of equity.
- Better-than-expected credit offtake.
- Improvements in the country's GDP growth outlook

Shareholding structure of banks

Fig.35: Ahli Bank

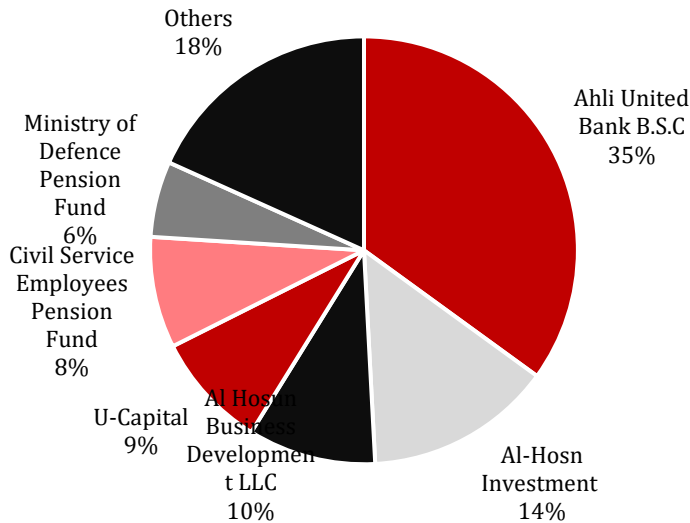


Fig.36: Bank Nizwa

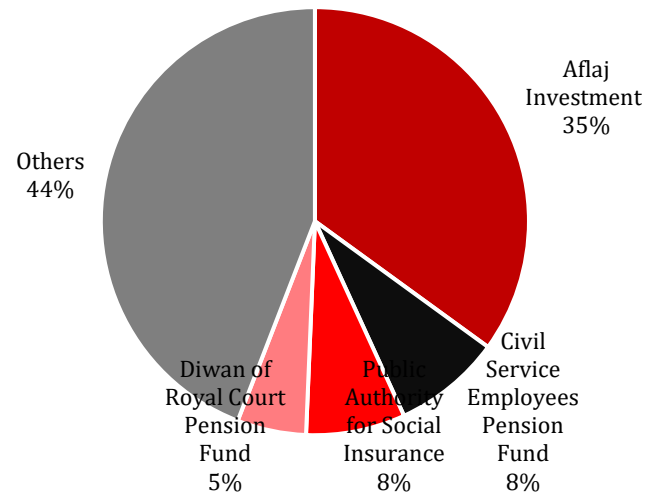


Fig.37: Bank Dhofar

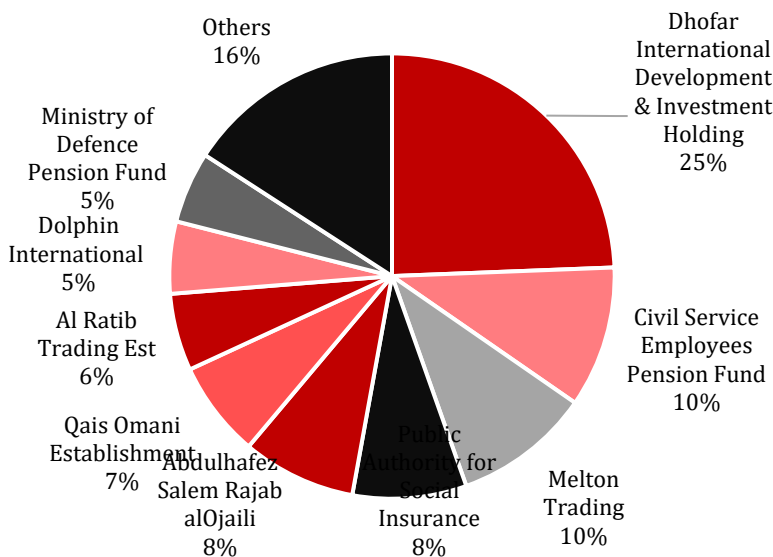


Fig.38: Oman Arab Bank

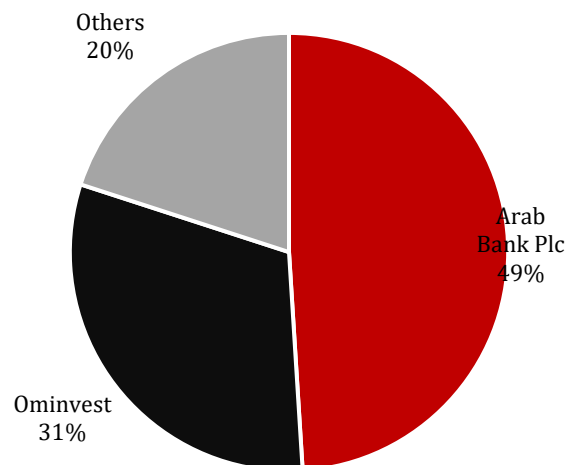


Fig.39: Sohar International Bank

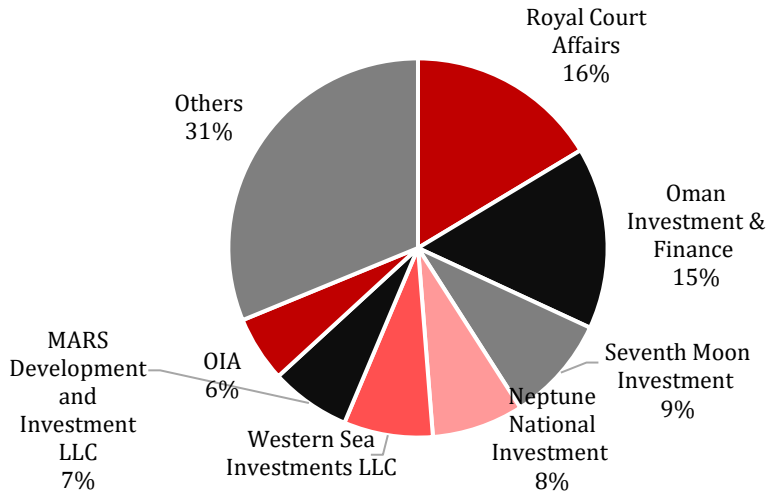


Fig.40: HSBC Bank Oman

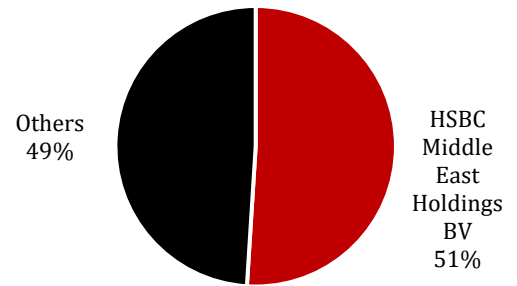


Fig. 41: National Bank of Oman

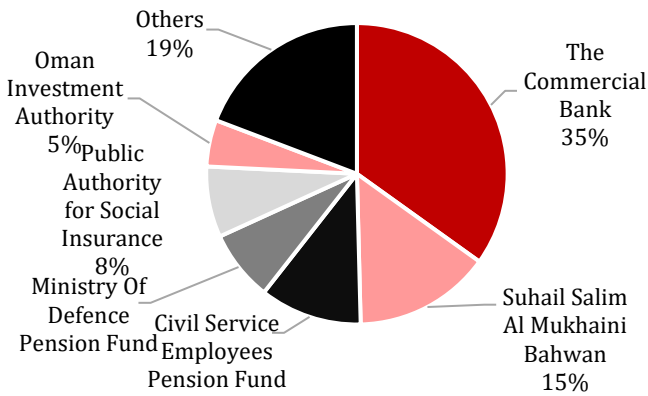
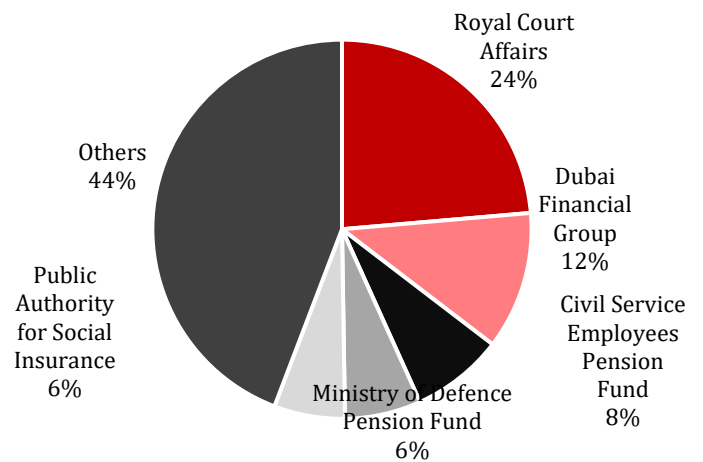


Fig.42: Bank Muscat



Source: MCD

Ahli Bank

Recommendation: Hold
Target Price: OMR 0.205
Upside/ (Downside): 2.5%

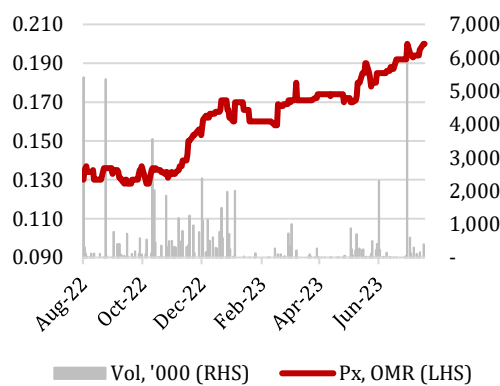
| | |
|---------------------------------|-------------|
| Rating | Hold |
| Target Price (TP), OMR | 0.205 |
| Bloomberg Ticker | ABOB OM |
| Current Market Price (OMR) | 0.200 |
| 52wk High / Low (OMR) | 0.200/0.130 |
| 12m Average Vol. (000) | 306 |
| Mkt. Cap. (USD/OMR Mn) | 1,014/390 |
| Shares Outstanding (mn) | 1,950 |
| Free Float (%) | 56% |
| 3m Avg Daily Turnover (OMR'000) | 47.4 |
| 6m Avg Daily Turnover (OMR'000) | 28.5 |
| P/E'23e (x) | 10.7 |
| P/B'23e (x) | 1.2 |
| Cash Dividend Yield '23e (%) | 5.0% |

Price Performance:

| | |
|--------------|----|
| 1 month (%) | 7 |
| 3 month (%) | 15 |
| 12 month (%) | 54 |

Source: Bloomberg

Price-Volume Performance



Source: Bloomberg

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- **Ahli Bank currently has the highest corporate lending exposure (c.70%) among banks in Oman which bodes well for the NIM expansion in the higher interest rate environment.**
- **The Bank has been a takeover target for both Bank Dhofar and Oman Arab Bank (through OMINVEST consortium)**
- **Ahli Bank has high footprint in Islamic Banking which has demonstrated high growth in the recent years**

We assign 'Hold' rating to Ahli Bank with a target price of OMR 0.205 based on company fundamentals and outlook. Ahli Bank is currently trading at a P/B of 1.2x on our 2023 estimates, compared to its peer average P/B, 2023e of 0.92x. We see a limited upside of 2.5% from current levels owing to the recent rally in ABOB stock coming from potential acquisition bids. Our valuation suggests a fair value of OMR 0.205/ share (target price), implying a 2.5% upside.

Investment Summary

In our view, for Ahli Bank: (1) earnings growth will continue given the positive macroeconomic environment owing to its high corporate exposure which should aid expansion of NIMs, (2) the bank has shown consistent performance with no surprises, (3) superior-than-sector average ROE justifies a higher P/B multiple as compared to some peers. The only caveat is a low CET1 ratio (despite being above regulatory threshold) might negatively affect dividend pay-out for the forecast period. We factor in slower net loan growth for Ahli Bank, given the current CET1 ratio, at a conservative CAGR of 5%. The cost-to-income ratio was reported at a historical low of 36.6% in 2Q23, which in our view may not be sustainable going forward. We include a stable 43% cost to income ratio in our estimates. Given the high interest rate environment, ABOB could decide to undertake higher provisions to improve its provision coverage.

2Q23 earnings summary

Solid set of results reported ahead of U Capital estimates. We believe the beat is owing to higher corporate loan book exposure, which would've helped expansion in NIMs. The cost-to-income ratio further improved in 2Q23. ABOB posted 40%YoY increase in its net profit for 2Q23 at OMR 11.6mn. Net profit beat is attributed to a solid operating income supported by lower expenses despite higher-than-expected net ECL charges in the quarter. The bank's net loans & Islamic financing portfolio expanded by 7%YoY and customer deposits grew 9%YoY. Loan to deposit ratio expanded to 110.4% in 2Q23 vs. 109.9% in 1Q23.

Key Indicators

| Year | FY-20 | FY-21 | FY-22 | FY-23e | FY-24e | FY-25e |
|----------------------------------|-------|-------|-------|--------|--------|--------|
| Total Net Loans (OMR mn) | 2,219 | 2,402 | 2,500 | 2,625 | 2,756 | 2,896 |
| Total Customer Deposits (OMR mn) | 2,181 | 2,296 | 2,499 | 2,626 | 2,763 | 2,909 |
| Operating Income (OMR mn) | 71 | 82 | 92 | 93 | 96 | 99 |
| Net Profit (OMR mn) | 24 | 28 | 33 | 35 | 37 | 38 |
| Diluted EPS (OMR) | 0.015 | 0.014 | 0.017 | 0.018 | 0.019 | 0.020 |
| Diluted BVPS (OMR) | 0.160 | 0.155 | 0.160 | 0.163 | 0.166 | 0.169 |
| P/E (x) | 8.7 | 8.2 | 11.8 | 11.1 | 10.6 | 10.2 |
| P/BVPS (x) | 0.8 | 0.7 | 1.3 | 1.2 | 1.2 | 1.2 |
| Dividend Yield | 3.9% | 6.5% | 4.5% | 4.8% | 5.0% | 5.2% |

Source: Company Financials, U Capital Research

* Market price for the current and subsequent years as per the latest closing price of 24-Jul-2023

Key Financials

| (OMR mn) | FY-20 | FY-21 | FY-22 | FY-23e | FY-24e | FY-25e |
|---|--------------|--------------|--------------|--------------|--------------|--------------|
| Income Statement | | | | | | |
| Interest/Financing Income | 131 | 141 | 151 | 157 | 166 | 175 |
| Interest Expense/Payment to Depositors | (71) | (76) | (77) | (82) | (90) | (97) |
| Net Interest/Financing Income | 60 | 66 | 74 | 75 | 77 | 79 |
| Fee & Commission Income | 8 | 9 | 10 | 10 | 10 | 11 |
| Other Income | 11 | 17 | 18 | 18 | 19 | 20 |
| Total Non-Interest/Financing Income | 11 | 17 | 18 | 18 | 19 | 20 |
| Total Operating Income | 71 | 82 | 92 | 93 | 96 | 99 |
| Operating Expenses | (30) | (36) | (40) | (41) | (42) | (43) |
| Operating Profit | | | | | | |
| Provisions expense | (14) | (15) | (13) | (11) | (11) | (12) |
| Profit Before Taxation | 27 | 32 | 38 | 41 | 43 | 44 |
| Taxation | (3) | (5) | (5) | (6) | (6) | (6) |
| Net Profit | 24 | 28 | 33 | 35 | 37 | 38 |
| Interest on Tier 1 Perpetual Securities | (9) | (9) | (9) | (11) | (11) | (11) |
| Net Profit Attributable to shareholders | 15 | 18 | 24 | 24 | 26 | 27 |
| Balance Sheet | | | | | | |
| Cash Balances | 79 | 115 | 132 | 196 | 191 | 187 |
| Deposits with Banks & FIs | 46 | 45 | 75 | 105 | 110 | 116 |
| Net Loans & Islamic financing | 2,219 | 2,402 | 2,500 | 2,625 | 2,756 | 2,896 |
| Investments | 306 | 428 | 293 | 308 | 323 | 340 |
| Net Fixed Assets | 23 | 27 | 35 | 39 | 42 | 47 |
| Other Assets | 29 | 36 | 39 | 39 | 39 | 39 |
| Total Assets | 2,702 | 3,053 | 3,075 | 3,311 | 3,465 | 3,627 |
| Deposits from Banks & FIs | 135 | 262 | 223 | 243 | 255 | 269 |
| <i>Islamic Deposits</i> | 285 | 394 | 479 | 522 | 548 | 577 |
| <i>Conventional Deposits</i> | 1,639 | 1,788 | 1,817 | 1,977 | 2,078 | 2,186 |
| Total Customer Deposits | 1,925 | 2,181 | 2,296 | 2,499 | 2,626 | 2,763 |
| Other Borrowings | 172 | 95 | - | - | - | - |
| Other Liabilities | 82 | 86 | 95 | 103 | 109 | 114 |
| Total liabilities | 2,314 | 2,626 | 2,615 | 2,845 | 2,990 | 3,146 |
| Paid-up Capital | 165 | 195 | 195 | 195 | 195 | 195 |
| Retained Earnings | 47 | 60 | 68 | 70 | 72 | 75 |
| Other Reserves | 52 | 48 | 49 | 52 | 56 | 60 |
| Shareholders' Equity | 264 | 303 | 312 | 317 | 323 | 330 |
| Tier 1 Perpetual Notes | 124 | 124 | 149 | 149 | 149 | 149 |
| Total Equity & Liabilities | 2,702 | 3,053 | 3,075 | 3,311 | 3,463 | 3,625 |
| Cash Flow Statement | | | | | | |
| Cash from operations | 50 | 159 | (107) | 112 | 46 | 48 |
| Cash from investing activities | 50 | 126 | (127) | 18 | 19 | 21 |
| Cash from financing | (30) | 2 | (2) | (30) | (31) | (31) |
| Net changes in cash | (29) | 36 | 18 | 64 | (4) | (4) |
| Cash at the end of period | 79 | 115 | 132 | 196 | 191 | 187 |
| Key Ratios | | | | | | |
| Return on Average Assets | 0.9% | 1.0% | 1.1% | 1.1% | 1.1% | 1.1% |
| Return on Average Equity | 9.1% | 9.7% | 10.8% | 11.2% | 11.5% | 11.6% |
| Net Interest & Islamic Finance Income / Operating I | 84.1% | 79.5% | 80.5% | 80.6% | 80.1% | 79.8% |
| Other operating income / Operating Income | 15.9% | 20.5% | 19.5% | 19.4% | 19.9% | 20.2% |
| Net fee Income/Operating Income | 10.7% | 10.7% | 10.7% | 10.7% | 10.7% | 10.7% |
| Interest Earning/Financing Assets Yield | 5.3% | 5.2% | 5.3% | 5.3% | 5.3% | 5.4% |
| Cost of Funds | 2.6% | 2.3% | 2.0% | 2.0% | 2.1% | 2.1% |
| Net Spread | 2.7% | 2.9% | 3.3% | 3.3% | 3.3% | 3.2% |
| Cost to Income Ratio | 42% | 43% | 44% | 44% | 44% | 44% |
| Net Loans & Islamic Financing to Customer Deposit: | 115.3% | 110.1% | 108.9% | 105.1% | 105.0% | 104.8% |
| Non Performing Loans, OMR mn | 40 | 78 | 98 | 103 | 108 | 114 |
| NPLs to Gross Loans & Islamic financing | 1.7% | 3.2% | 3.8% | 3.8% | 3.8% | 3.8% |
| NPL Coverage, % | 148.0% | 98.1% | 90.8% | 91.0% | 91.1% | 91.3% |
| Cost of Risk, bps | 58.4 | 53.9 | 45.5 | 42.5 | 40.5 | 39.5 |
| Shareholders' Equity to Total Loans & Islamic Finan | 0.12 | 0.12 | 0.12 | 0.12 | 0.11 | 0.11 |
| Shareholders' Equity to Total Assets, x | 0.10 | 0.10 | 0.10 | 0.10 | 0.09 | 0.09 |
| Capital Adequacy Ratio, % | 15.7% | 16.7% | 16.3% | 15.4% | 15.0% | 15.1% |
| EPS, OMR | 0.015 | 0.014 | 0.017 | 0.018 | 0.019 | 0.020 |
| BVPS, OMR | 0.160 | 0.155 | 0.160 | 0.163 | 0.166 | 0.169 |
| Market Price, OMR* | 0.127 | 0.116 | 0.200 | 0.200 | 0.200 | 0.200 |
| Cash Dividend Payout Ratio, % | 34.4% | 53.0% | 53.0% | 53.0% | 53.0% | 53.0% |
| Cash Dividend Yield, % | 3.9% | 6.5% | 4.5% | 4.8% | 5.0% | 5.2% |
| P/E Ratio, x | 8.7 | 8.2 | 11.8 | 11.1 | 10.6 | 10.2 |
| P/BV Ratio, x | 0.8 | 0.7 | 1.3 | 1.2 | 1.2 | 1.2 |

*Market price for current year and subsequent years as per the closing price on 24-Jul-2023

Source: Company Financials

Bank Dhofar

Recommendation: Hold
Target Price: OMR 0.182
Upside/ (Downside): 4%

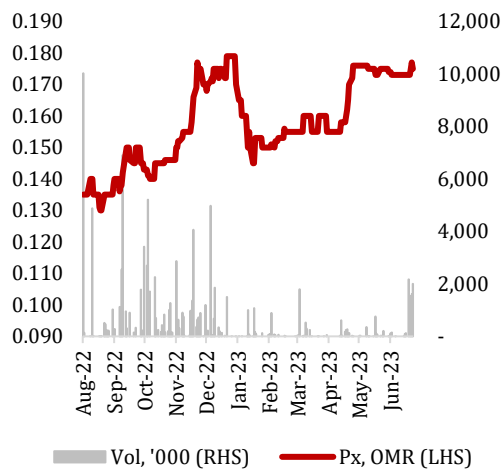
| | |
|----------------------------|-------------|
| Recommendation | Hold |
| Bloomberg Ticker | BKDB OM |
| Current Market Price (OMR) | 0.175 |
| 52wk High / Low (OMR) | 0.190/0.120 |
| 12m Average Vol. ('000) | 416.2 |
| Mkt. Cap. (USD/OMR Mn) | 1,363/524 |
| Shares Outstanding (mn) | 2,996.4 |
| Free Float (%) | 52% |
| 3m Avg Daily Turnover | 32.0 |
| 6m Avg Daily Turnover | 24.4 |
| P/E '23e (x) | 12.5 |
| P/B '23e (x) | 0.90 |
| Dividend Yield '23e(%) | 3.2% |

Price Performance:

| | |
|--------------|------|
| 1 month (%) | 1.2 |
| 3 month (%) | 12.9 |
| 12 month (%) | 36.7 |

Source: Bloomberg, values as of 24 July 2023

Price-Volume Performance



Source: Bloomberg

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- **Bank Dhofar currently is the second largest bank in Oman with a market share of c.11.4% of total assets and 10.8% on total deposits**
- **Capital Adequacy Ratio of 19.3% as of end-1Q23; 73% NPL coverage ratio as of 1Q23**
- **Bank is currently looking to expand inorganically through acquisition of Ahli Bank and has launched an open offer for the same**

We assign 'Hold' rating to Bank Dhofar with a target price of OMR 0.182 based on company fundamentals and outlook. Currently, the stock trades at a P/BV of 0.9x based on our FY 2023 estimates, broadly in line with the peer average P/BV of 0.92x. We see limited upside from current levels due to the recent rally in the stock price. The stock has been up 12.9% over the last three months and is currently trading at OMR 0.175. Our valuation suggests a fair value of OMR 0.182/ share (target price), implying a 4% upside.

Investment Summary

Benefiting from the continued fiscal reforms and healthy oil revenues in Oman, the regional Banking Sector is expected to see boost in credit growth. BKDB's NIM has improved recently due to the new management's focus on better pricing of assets as well as shedding of legacy high-cost deposits, however, Bank Dhofar currently has the lowest level of CASA ratio among Omani Banks, which pressures NIMs. Provision coverage is among the lowest in the sector with 73% coverage of non-performing assets. While cost of risk is expected to peak in 2022, it is likely to remain close to 90bps on gross loans for the bank to improve provision coverage further.

2Q23 earnings summary

Bank Dhofar posted a net profit of OMR 8.4mn for 2Q23, 3% above our estimate. Operating income was largely flat YoY for the quarter but down 5% QoQ. Operating expenses fell 4% YoY and 3% QoQ, landing 10% better than our estimate. Operating profit is 8% ahead of our estimate on lower expenses for the quarter. For 1H23, BKDB has reported a 3.5% decline in Net Interest Income owing to pressure on NIMs during the period due to high cost of deposits. The bank has posted net ECL charges of OMR 9.7mn, which is 14% above our estimate. The charges were up 18% YoY and 7% QoQ. For 1H23, net ECL charges rose 15% YoY as the bank appears to be building provision buffers.

Key Indicators

| Year | FY-20 | FY-21 | FY-22 | FY-23e | FY-24e | FY-25e |
|----------------------------------|-------|-------|-------|--------|--------|--------|
| Total Net Loans (OMR mn) | 3,265 | 3,346 | 3,430 | 3,626 | 3,833 | 4,047 |
| Total Customer Deposits (OMR mn) | 2,861 | 2,976 | 3,054 | 3,231 | 3,418 | 3,612 |
| Operating Income (OMR mn) | 130 | 126 | 143 | 158 | 168 | 180 |
| Net Profit (OMR mn) | 31 | 25 | 33 | 42 | 47 | 54 |
| Diluted EPS (OMR) | 0.010 | 0.008 | 0.011 | 0.014 | 0.016 | 0.018 |
| Diluted BVPS (OMR) | 0.180 | 0.181 | 0.187 | 0.194 | 0.200 | 0.209 |
| P/E (x) | 9.5 | 14.9 | 11.3 | 12.5 | 11.1 | 9.7 |
| P/BV (x) | 0.54 | 0.69 | 0.67 | 0.90 | 0.87 | 0.84 |
| Dividend Yield (%) | 4.1% | 1.6% | 3.1% | 3.2% | 3.6% | 4.1% |

Source: Company Financials, U Capital Research

Key Financials

| (OMR mn) | FY20 | FY21 | FY-22 | FY-23e | FY-24e | FY-25e |
|--|--------------|--------------|--------------|--------------|--------------|--------------|
| Income Statement | | | | | | |
| Interest/Financing Income | 205 | 207 | 221 | 236 | 253 | 272 |
| Interest Expense/Payment to Depositors | (98) | (104) | (99) | (104) | (113) | (121) |
| Net Interest/Financing Income | 108 | 102 | 122 | 132 | 140 | 151 |
| Fee & Commission Income | 14 | 15 | 13 | 14 | 15 | 15 |
| Other Income | 9 | 9 | 7 | 12 | 13 | 14 |
| Total Non-Interest/Financing Income | 22 | 24 | 21 | 26 | 28 | 29 |
| Total Operating Income | 130 | 126 | 143 | 158 | 168 | 180 |
| Operating Expenses | (65) | (72) | (70) | (73) | (75) | (79) |
| Operating Profit | 65 | 54 | 73 | 85 | 93 | 101 |
| Provisions expense | (29) | (25) | (34) | (36) | (37) | (38) |
| Profit Before Taxation | 36 | 29 | 39 | 49 | 56 | 64 |
| Taxation & others | (5) | (4) | (6) | (7) | (8) | (10) |
| Net Profit | 31 | 25 | 33 | 42 | 47 | 54 |
| Interest on Tier 1 Perpetual Securities | (10) | (9) | (11) | (11) | (11) | (11) |
| Net Profit Attributable to shareholders | 20 | 16 | 22 | 31 | 36 | 43 |
| Balance Sheet | | | | | | |
| Cash Balances | 209 | 251 | 177 | 236 | 270 | 277 |
| Deposits with Banks & FIs | 122 | 125 | 148 | 211 | 190 | 199 |
| Net Loans & Islamic financing | 3,265 | 3,346 | 3,430 | 3,626 | 3,833 | 4,047 |
| Investments | 458 | 446 | 469 | 453 | 475 | 498 |
| Net Fixed Assets | 21 | 8 | 8 | 8 | 9 | 9 |
| Other Assets | 182 | 262 | 85 | 88 | 92 | 96 |
| Total Assets | 4,257 | 4,439 | 4,317 | 4,622 | 4,868 | 5,125 |
| Deposits from Banks & FIs | 452 | 461 | 573 | 500 | 529 | 560 |
| Total Customer Deposits | 2,861 | 2,976 | 3,054 | 3,231 | 3,418 | 3,612 |
| Other Borrowings | 35 | 35 | - | - | - | - |
| Other Liabilities | 213 | 269 | 136 | 155 | 164 | 173 |
| Total liabilities | 3,561 | 3,740 | 3,763 | 3,886 | 4,112 | 4,345 |
| Paid-up Capital | 300 | 300 | 300 | 300 | 300 | 300 |
| Retained Earnings | 34 | 29 | 72 | 88 | 104 | 125 |
| Other Reserves | 207 | 214 | 190 | 193 | 197 | 201 |
| Shareholders' Equity | 540 | 543 | 562 | 581 | 601 | 625 |
| Tier 1 Perpetual Notes | 156 | 156 | 156 | 156 | 156 | 156 |
| Total Equity & Liabilities | 4,257 | 4,439 | 4,480 | 4,622 | 4,868 | 5,125 |
| Cash Flow Statement | | | | | | |
| Cash from operations | 30 | 30 | (13) | 55 | 73 | 50 |
| Cash from investing activities | 82 | (25) | 23 | (16) | 22 | 23 |
| Cash from financing | (40) | (13) | (39) | (12) | (17) | (19) |
| Net changes in cash | (92) | 43 | (75) | 59 | 34 | 7 |
| Cash at the end of period | 209 | 251 | 177 | 236 | 270 | 277 |
| Key Ratios | | | | | | |
| Return on Average Assets | 0.7% | 0.6% | 0.8% | 0.9% | 1.0% | 1.1% |
| Return on Average Equity | 5.7% | 4.6% | 6.0% | 7.3% | 8.0% | 8.8% |
| Net Interest & Islamic Finance Income / Operating Income | 82.8% | 81.0% | 85.5% | 83.4% | 83.6% | 83.8% |
| Other operating income / Operating Income | 17.2% | 19.0% | 14.5% | 16.6% | 16.4% | 16.2% |
| Net fee Income/Operating Income | 10.5% | 12.2% | 9.3% | 8.8% | 8.8% | 8.6% |
| Interest Earning/Financing Assets Yield | 5.29% | 5.33% | 5.56% | 5.65% | 5.77% | 5.88% |
| Cost of Funds | 2.85% | 3.06% | 2.86% | 2.90% | 2.94% | 2.98% |
| Net Spread | 2.44% | 2.27% | 2.69% | 2.75% | 2.82% | 2.90% |
| Cost to Income Ratio | 50.1% | 57.2% | 48.7% | 46.0% | 44.9% | 43.7% |
| Net Loans & Islamic Financing to Customer Deposits (Total LTI) | 114.1% | 112.5% | 112.3% | 112.2% | 112.1% | 112.0% |
| Non Performing Loans, OMR mn | 154 | 180 | 208 | 216 | 224 | 233 |
| NPLs to Gross Loans & Islamic financing | 4.5% | 5.1% | 5.7% | 5.6% | 5.5% | 5.4% |
| NPL Coverage, % | 93.4% | 93.3% | 104.0% | 107.3% | 110.7% | 114.2% |
| Cost of Risk, bps | 74.7 | 63.5 | 86.2 | 86.2 | 84.2 | 81.2 |
| Shareholders' Equity to Total Loans & Islamic Financing, x | 0.16 | 0.15 | 0.15 | 0.15 | 0.15 | 0.14 |
| Shareholders' Equity to Total Assets, x | 0.15 | 0.15 | 0.16 | 0.15 | 0.15 | 0.14 |
| Capital Adequacy Ratio, % | 17.7% | 17.7% | 17.4% | 16.9% | 16.4% | 16.1% |
| EPS, OMR | 0.010 | 0.008 | 0.011 | 0.014 | 0.016 | 0.018 |
| BVPS, OMR | 0.180 | 0.181 | 0.187 | 0.194 | 0.200 | 0.209 |
| Market Price, OMR* | 0.097 | 0.125 | 0.125 | 0.175 | 0.175 | 0.175 |
| Cash Dividend Payout Ratio, % | 39.2% | 23.9% | 35.0% | 40.0% | 40.0% | 40.0% |
| Cash Dividend Yield, % | 4.1% | 1.6% | 3.1% | 3.2% | 3.6% | 4.1% |
| P/E Ratio, x | 9.5 | 14.9 | 11.3 | 12.5 | 11.1 | 9.7 |
| P/BV Ratio, x | 0.54 | 0.69 | 0.67 | 0.90 | 0.87 | 0.84 |

*Market price for current year and subsequent years as per the closing price on 24-Jul-2023

Source: Company Financials, U Capital Research

Recommendation: Accumulate
Target Price: 0.310
Upside/ (Downside): 10.7%

Bank Muscat

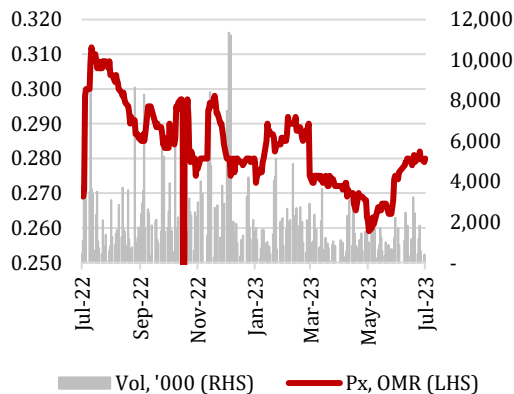
| | |
|------------------------------|-------------------|
| Recommendation | Accumulate |
| Bloomberg Ticker | BKMB OM |
| Current Market Price (OMR) | 0.280 |
| 52wk High / Low (OMR) | 0.320/0.150 |
| 12m Average Vol. (000) | 2,007.9 |
| Mkt. Cap. (USD/OMR mn) | 5,465/2,102 |
| Shares Outstanding (mn) | 7,506.4 |
| Free Float (%) | 76% |
| 3m Avg Daily Turnover | 335.2 |
| 6m Avg Daily Turnover | 384.8 |
| P/E'23e (x) | 9.7 |
| P/B'23e (x) | 1.1 |
| Cash Dividend Yield '23e (%) | 5.0% |

Price Performance:

| | |
|--------------|-----|
| 1 month (%) | 1.8 |
| 3 month (%) | 2.9 |
| 12 month (%) | 3.3 |

Source: Bloomberg, values as of 24 July 2023

Price-Volume Performance



Source: Bloomberg

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- **Bank Muscat is the largest bank in Oman with a market share of c.32.3% in terms of total asset base and 33% on total deposits**
- **Best-in-class Capitalization metrics: Capital Adequacy Ratio of 21.3% as of end-1Q23, well ahead of peers**
- **Strong outlook on most core line-items, including NIM expansion, balance sheet growth, stable asset quality, and higher contribution from core non-funded income to all support earnings growth**

We maintain 'Accumulate' on Bank Muscat based on company fundamentals and outlook. Currently, the stock trades at a P/BV of 1.1x based on our FY 2023 estimates, above the peer average P/BV of 0.92x. The stock has been up 1.8% over the last month and is currently trading at OMR 0.280. Our valuation suggests a fair value of OMR0.310/ share (target price), implying a 10.7% upside.

Investment Summary

Benefiting from the continued fiscal reforms and healthy oil revenues in Oman, the regional Banking Sector is expected to see boost in credit growth. Bank Muscat, being the largest bank in Oman, is well-positioned to take advantage of higher credit offtake. Consequently, we anticipate an operating income growth of approx. 6% CAGR over 2023-2027E. BKMB benefits from its significant low-cost deposit base (66.3% CASA ratio as of end-1Q23) which will drive net interest margin (NIM) expansion in the short to medium term. We note the high NPL coverage ratio (163% as of FY2022) and believe expected credit loss (ECL) allowance charges should taper as the pandemic related delinquencies come to an end. We have built in a growth expectation for net profit at a CAGR of 6% over 2023-2027e.

2Q23 earnings summary

2Q23 continued the solid momentum of 1Q23 which was a solid start to the year. Bank Muscat posted a net profit of OMR 53mn in 2Q23, up by 4%YoY. Net profit for 1H23 is higher by 5% YoY. The bank's operating expenses declined 6%YoY and flat QoQ and Cost to income ratio reported was a record low at 38.1%. We are encouraged with the consistent progress on the cost-to-income ratio and forecast group net profit growth of 8.2% for 2023e (driven by tapering cost of risk) and 4.7% for 2024e translating into RoE of 12.2%/ 12.0% for 2023e/ 2024e.

Key Indicators

| Year | FY20 | FY21 | FY22 | FY23e | FY24e | FY25e |
|----------------------------------|-------|-------|-------|-------|--------|--------|
| Total Net Loans (OMR mn) | 8,983 | 9,191 | 9,417 | 9,813 | 10,304 | 10,922 |
| Total Customer Deposits (OMR mn) | 8,459 | 8,775 | 8,647 | 9,032 | 9,535 | 10,054 |
| Operating Income (OMR mn) | 457 | 475 | 503 | 526 | 549 | 579 |
| Net Profit (OMR mn) | 163 | 190 | 201 | 217 | 227 | 240 |
| Diluted EPS (OMR) | 0.050 | 0.053 | 0.027 | 0.029 | 0.030 | 0.032 |
| Diluted BVPS (OMR) | 0.589 | 0.565 | 0.230 | 0.244 | 0.260 | 0.278 |
| P/E (x) | 7.8 | 9.1 | 10.2 | 9.0 | 8.5 | 8.1 |
| P/BVPS (x) | 0.7 | 0.9 | 1.2 | 1.1 | 1.0 | 0.9 |
| Dividend Yield (%) | 6.3% | 6.2% | 5.5% | 5.4% | 5.7% | 6.0% |

Source: Company Financials, U Capital Research

| Key Financials (OMR mn) | FY20 | FY21 | FY22 | FY23e | FY24e | FY25e |
|---|---------------|---------------|---------------|---------------|---------------|---------------|
| Income Statement | | | | | | |
| Interest/Financing Income | 506.0 | 521.8 | 553.8 | 575.1 | 606.2 | 644.6 |
| Interest Expense/Payment to Depositors | (183.9) | (186.3) | (208.9) | (216.0) | (231.2) | (248.2) |
| Net Interest/Financing Income | 322.1 | 335.5 | 344.9 | 359.1 | 375.1 | 396.3 |
| Fee & Commission Income | 90.3 | 99.9 | 110.0 | 115.0 | 120.1 | 126.3 |
| Other Income | 44.1 | 40.0 | 47.9 | 51.6 | 53.9 | 56.7 |
| Total Non-Interest/Financing Income | 134.4 | 139.9 | 158.0 | 166.6 | 174.0 | 183.0 |
| Total Operating Income | 456.5 | 475.5 | 502.8 | 525.6 | 549.1 | 579.3 |
| Operating Expenses | (179.9) | (191.5) | (207.3) | (218.3) | (229.7) | (244.1) |
| Operating Profit | 276.7 | 284.0 | 295.5 | 307.3 | 319.4 | 335.3 |
| Provisions expense | (81.0) | (60.1) | (59.0) | (51.5) | (51.5) | (53.0) |
| Profit Before Taxation | 195.6 | 224.0 | 236.5 | 255.9 | 267.9 | 282.3 |
| Taxation & others | (32.3) | (34.3) | (35.7) | (38.7) | (40.5) | (42.7) |
| Net Profit Attributable to Parent | 163.4 | 189.6 | 200.8 | 217.2 | 227.4 | 239.6 |
| Interest of Tier 1 Perpetual Securities | (7.2) | (7.2) | (7.2) | (23.1) | (23.1) | (23.1) |
| Net Profit Attributable to shareholders | 156.2 | 182.5 | 193.6 | 194.1 | 204.3 | 216.5 |
| Balance Sheet | | | | | | |
| Cash Balances | 657 | 1,047 | 883 | 882 | 1,049 | 1,027 |
| Deposits with Banks & FIs | 575 | 765 | 641 | 713 | 674 | 698 |
| <i>Gross Loans (Conventional)</i> | <i>8,093</i> | <i>8,255</i> | <i>8,467</i> | <i>8,805</i> | <i>9,246</i> | <i>9,800</i> |
| <i>Loan Loss Reserve (Conventional)</i> | <i>(362)</i> | <i>(425)</i> | <i>(499)</i> | <i>(519)</i> | <i>(545)</i> | <i>(578)</i> |
| Net Loans (Conventional) | 7,731 | 7,830 | 7,967 | 8,286 | 8,700 | 9,223 |
| <i>Gross Islamic Financing</i> | <i>1,285</i> | <i>1,405</i> | <i>1,508</i> | <i>1,568</i> | <i>1,647</i> | <i>1,745</i> |
| <i>Loan Loss Reserve (Islamic)</i> | <i>(34)</i> | <i>(44)</i> | <i>(59)</i> | <i>(41)</i> | <i>(43)</i> | <i>(46)</i> |
| Net Islamic Financing | 1,251 | 1,361 | 1,449 | 1,527 | 1,603 | 1,699 |
| <i>Gross Loans & Islamic financing</i> | <i>9,379</i> | <i>9,660</i> | <i>9,975</i> | <i>10,374</i> | <i>10,892</i> | <i>11,546</i> |
| <i>Loan Loss Reserve (Conventional + Islamic)</i> | <i>(396)</i> | <i>(469)</i> | <i>(558)</i> | <i>(561)</i> | <i>(589)</i> | <i>(624)</i> |
| Net Loans & Islamic financing | 8,983 | 9,191 | 9,417 | 9,813 | 10,304 | 10,922 |
| Investments | 1,847 | 1,811 | 1,572 | 1,638 | 1,720 | 1,823 |
| Net Fixed Assets | 71 | 74 | 68 | 71 | 71 | 70 |
| Other Assets | 321 | 183 | 194 | 193 | 203 | 215 |
| Total Assets | 12,454 | 13,073 | 12,776 | 13,311 | 14,020 | 14,756 |
| Deposits from Banks & FIs | 940 | 1,218 | 1,004 | 1,049 | 1,107 | 1,168 |
| <i>Islamic Deposits</i> | <i>1,030</i> | <i>1,171</i> | <i>1,237</i> | <i>1,308</i> | <i>1,373</i> | <i>1,454</i> |
| <i>Conventional Deposits</i> | <i>7,429</i> | <i>7,604</i> | <i>7,410</i> | <i>7,724</i> | <i>8,162</i> | <i>8,601</i> |
| Total Customer Deposits | 8,459 | 8,775 | 8,647 | 9,032 | 9,535 | 10,054 |
| Other Borrowings | 494 | 481 | 436 | 436 | 436 | 436 |
| Other Liabilities | 518 | 448 | 457 | 457 | 482 | 508 |
| Total liabilities | 10,410 | 10,922 | 10,544 | 10,974 | 11,561 | 12,167 |
| Paid-up Capital | 325 | 357 | 751 | 751 | 751 | 751 |
| Retained Earnings | 538 | 595 | 268 | 372 | 431 | 491 |
| Other Reserves | 1,051 | 1,069 | 708 | 709 | 772 | 842 |
| Shareholders' Equity | 1,914 | 2,021 | 1,727 | 1,832 | 1,954 | 2,084 |
| Minority Interest, Tier 1 Perpetual Notes | 130 | 130 | 505 | 505 | 505 | 505 |
| Total Equity & Liabilities | 12,454 | 13,073 | 12,776 | 13,311 | 14,020 | 14,756 |
| Cash Flow Statement | | | | | | |
| Cash from operations | 2 | 497 | (5) | 106 | 272 | 87 |
| Cash from investing activities | (8) | 11 | (5) | (6) | (0) | (1) |
| Cash from financing | (135) | (96) | (164) | (112) | (105) | (110) |
| Net changes in cash | (125) | 390 | (164) | (1) | 167 | (22) |
| Cash at the end of period | 657 | 1,047 | 883 | 882 | 1,049 | 1,027 |
| Key Ratios | | | | | | |
| Return on Average Assets | 1.3% | 1.5% | 1.6% | 1.7% | 1.7% | 1.7% |
| Return on Average Equity | 8.6% | 9.6% | 10.7% | 12.2% | 12.0% | 11.9% |
| Net Interest Income & Islamic Finance Income/ Operati | 70.6% | 70.6% | 68.6% | 68.3% | 68.3% | 68.4% |
| Other Operating Income/Operating Income | 29.4% | 29.4% | 31.4% | 31.7% | 31.7% | 31.6% |
| Net fee income/Operating Income | 19.8% | 21.0% | 21.9% | 21.9% | 21.9% | 21.8% |
| Interest Earning/Finance Asset Yield | 4.5% | 4.5% | 4.7% | 4.8% | 4.9% | 4.9% |
| Cost of Funds | 1.9% | 1.8% | 2.0% | 2.1% | 2.1% | 2.2% |
| Net Spread | 2.6% | 2.7% | 2.7% | 2.7% | 2.7% | 2.7% |
| Cost to Income Ratio | 39.4% | 40.3% | 41.2% | 41.5% | 41.8% | 42.1% |
| Net Loans & Islamic Financing to Customer Deposits (T | 106% | 105% | 109% | 109% | 108% | 109% |
| Non Performing Loans, OMR mn | 338 | 356 | 371 | 386 | 405 | 430 |
| NPLs to Gross Loans & Islamic Financing, % | 3.6% | 3.7% | 3.7% | 3.7% | 3.7% | 3.7% |
| NPL Coverage, % | 117.3% | 131.5% | 163.0% | 145.3% | 145.3% | 145.3% |
| Cost of Risk (bps) | 87.3 | 63.3 | 61.1 | 57.9 | 54.4 | 50.7 |
| Shareholders' Equity to Total Loans & Islamic Financing | 0.20 | 0.21 | 0.17 | 0.18 | 0.18 | 0.18 |
| Shareholders' Equity to Total Assets, x | 0.15 | 0.15 | 0.14 | 0.14 | 0.14 | 0.14 |
| Capital Adequacy Ratio, % | 20.8% | 21.3% | 21.3% | 21.3% | 21.5% | 21.3% |
| EPS (OMR) | 0.050 | 0.053 | 0.027 | 0.029 | 0.030 | 0.032 |
| BVPS (OMR) | 0.589 | 0.565 | 0.230 | 0.244 | 0.260 | 0.278 |
| Market Price (OMR) * | 0.394 | 0.484 | 0.273 | 0.280 | 0.280 | 0.280 |
| Cash Dividend Payout Ratio, % | 49.7% | 56.6% | 56.1% | 48.3% | 48.5% | 48.8% |
| Cash Dividend Yield, % | 6.3% | 6.2% | 5.5% | 5.0% | 5.2% | 5.6% |
| P/E Ratio (x) | 7.8 | 9.1 | 10.2 | 9.7 | 9.2 | 8.8 |
| P/BV Ratio (x) | 0.7 | 0.9 | 1.2 | 1.1 | 1.1 | 1.0 |

*Market price for current year and subsequent years as per the closing price on 24-Jul-2023

Source: Company Financials, U Capital Research

National Bank of Oman

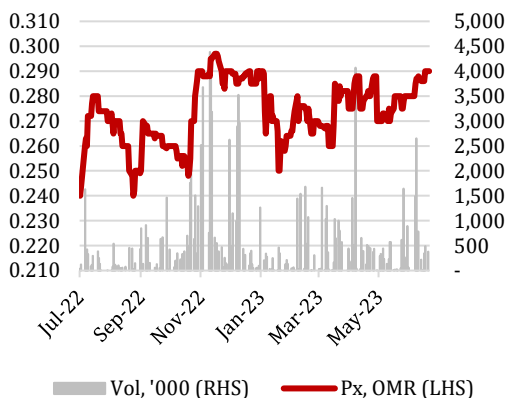
Recommendation: Accumulate
Target Price: 0.330
Upside/ (Downside): 10.4%

| Recommendation | Accumulate |
|---------------------------------|-------------|
| Bloomberg Ticker | NBOB OM |
| Current Market Price (OMR) | 0.299 |
| 52wk High / Low (OMR) | 0.300/0.230 |
| 12m Average Vol. (000) | 435.7 |
| Mkt. Cap. (USD/OMR Mn) | 1,264/486 |
| Shares Outstanding (mn) | 1,625.9 |
| Free Float (%) | 27% |
| 3m Avg Daily Turnover (OMR'000) | 114.3 |
| 6m Avg Daily Turnover (OMR'000) | 100.3 |
| P/E'23e (x) | 7.4 |
| P/B'23e (x) | 0.95 |
| Cash Dividend Yield '23e (%) | 6% |

| Price Performance: | |
|--------------------|------|
| 1 month (%) | 6.8 |
| 3 month (%) | 6.0 |
| 12 month (%) | 24.6 |

Source: Bloomberg

Price-Volume Performance



Source: Bloomberg

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- **NBO has made significant progress in improving cost efficiency.**
- **Sound Capital Adequacy ratios : 16.9% CAR as of 1Q23**
- **Improving asset quality metrics; Cost of risk seems to have peaked, but provision cover slightly below 100%**
- **Loan book skewed towards retail, unlike peers except Bank Muscat, with retail at 40% vs. peers at a simple average of 36%**

We assign Accumulate rating to the stock, with an updated target price of OMR 0.330, implying an upside of 10.1%. NBO is currently trading at a P/B of 0.97x, compared to peer average of 0.92x. the stock has performed considerably well over the last 12-months; however, we still further upside potential from current levels.

Investment summary

NBO's loan book is skewed towards retail, unlike peers except Bank Muscat, with retail at 40% vs. peers at a simple average of 36%. We believe that NBO's cost of risk has peaked, but we expect it to remain elevated this year as the bank improves its provision cover which is currently below 100%. The bank could potentially see improvement in its earnings as efficiency is expected to improve and cost of risk is expected to decline from 2023e.

2Q23 earnings summary

Results reported were in line with U Capital estimates. The bank posted a 26%YoY and 4% QoQ increase in its net profit for 2Q23 at OMR 15mn, in line with our estimate for the quarter. The bank posted 11%YoY growth and 2%QoQ decline in its net interest income, which is 7% below our estimate. The operating income increased a solid 26%YoY and 3%QoQ. Total operating income reached OMR37.6mn, up 15%YoY and down 1%QoQ, landing in line with our estimate for the quarter.

Net ECL provision charge is up 6%YoY and down 22%QoQ, 16% better than our estimate. The bank has posted an increase in net loans & Islamic financing of 12%YoY (+1% QoQ), in line with our estimate. Customer deposits are up 9%YoY and 2%QoQ. Loan-to-deposit ratio declined to 104.2% in 2Q23 vs. 105.1% in 1Q23, on loan growth outpacing deposit growth YoY and is higher than 101.5% recorded a year ago.

Key Indicators

| Year | FY20 | FY21 | FY22 | FY23e | FY24e | FY25e |
|----------------------------------|-------|-------|-------|-------|-------|-------|
| Total Net Loans (OMR mn) | 2,888 | 3,089 | 3,354 | 3,683 | 4,045 | 4,362 |
| Total Customer Deposits (OMR mn) | 2,527 | 2,918 | 3,047 | 3,412 | 3,711 | 4,021 |
| Operating Income (OMR mn) | 117 | 123 | 138 | 157 | 174 | 190 |
| Net Profit (OMR mn) | 18 | 30 | 48 | 64 | 76 | 88 |
| Diluted EPS (OMR) | 0.011 | 0.019 | 0.030 | 0.039 | 0.047 | 0.054 |
| Diluted BVPS (OMR) | 0.255 | 0.271 | 0.291 | 0.305 | 0.322 | 0.344 |
| P/E (x)* | 14.3 | 10.5 | 10.1 | 7.6 | 6.4 | 5.5 |
| P/BVPS (x)* | 0.63 | 0.72 | 1.03 | 0.98 | 0.93 | 0.87 |
| Dividend Yield (%)* | 0.0% | 1.9% | 3.5% | 5.9% | 7.0% | 8.2% |

Source: Bank Financials, U Capital Research

* Market price for the current and subsequent years as per the latest closing price

Key Financials

| (OMR mn) | 2020 | 2021 | 2022 | 2023e | 2024e | 2025e |
|--|---------------|---------------|---------------|---------------|---------------|---------------|
| Income Statement | | | | | | |
| Interest & Islamic Financing Income | 172.1 | 175.3 | 194.0 | 216.4 | 240.7 | 264.6 |
| Interest Expense & Payment to Depositors | (81.2) | (83.7) | (90.5) | (98.5) | (110.3) | (121.9) |
| Net Interest/Financing Income | 90.9 | 91.6 | 103.5 | 117.9 | 130.4 | 142.8 |
| Fee & Commission Income | 12.9 | 18.9 | 20.6 | 25.2 | 30.7 | 37.4 |
| Other Income | 13.1 | 12.9 | 14.1 | 14.4 | 12.8 | 9.9 |
| Total Non-Interest/Financing Income | 26.1 | 31.8 | 34.7 | 39.6 | 43.5 | 47.3 |
| Total Operating Income | 117.0 | 123.4 | 138.2 | 157.5 | 173.9 | 190.1 |
| Operating Expenses | (63.8) | (63.5) | (60.5) | (62.3) | (64.2) | (66.1) |
| Operating Profit | 53.1 | 59.9 | 77.7 | 95.1 | 109.7 | 124.0 |
| Provisions expense | (31.3) | (24.0) | (20.2) | (22.0) | (23.3) | (23.4) |
| Profit Before Taxation | 21.8 | 35.9 | 57.5 | 73.2 | 86.4 | 100.6 |
| Taxation | (3.7) | (5.6) | (9.3) | (9.2) | (10.7) | (12.3) |
| Net Profit | 18.1 | 30.3 | 48.2 | 64.0 | 75.7 | 88.2 |
| Interest on Tier 1 Perpetual Securities | (9.1) | (9.2) | (13.4) | (13.4) | (13.4) | (13.4) |
| Net Profit Attributable to shareholders | 9.1 | 20.8 | 34.6 | 50.6 | 62.3 | 74.9 |
| Balance Sheet | | | | | | |
| Cash Balances | 216 | 308 | 262 | 294 | 232 | 241 |
| Deposits with Banks & FIs | 95 | 115 | 119 | 159 | 175 | 188 |
| Net Loans & Islamic financing | 2,888 | 3,089 | 3,354 | 3,683 | 4,045 | 4,362 |
| Investments | 319 | 447 | 404 | 424 | 466 | 502 |
| Net Fixed Assets | 63 | 60 | 57 | 59 | 61 | 62 |
| Other Assets | 3,259 | 3,599 | 3,856 | 4,215 | 4,629 | 4,992 |
| Total Assets | 3,633 | 4,081 | 4,294 | 4,727 | 5,097 | 5,483 |
| Deposits from Banks & FIs | 289 | 298 | 262 | 293 | 319 | 345 |
| Total Customer Deposits | 2,527 | 2,918 | 3,047 | 3,412 | 3,711 | 4,021 |
| Other Borrowings | 308 | 308 | 356 | 356 | 356 | 356 |
| Other Liabilities | 94 | 118 | 155 | 170 | 187 | 202 |
| Total liabilities | 3,102 | 3,526 | 3,653 | 4,064 | 4,406 | 4,757 |
| Paid-up Capital | 163 | 163 | 163 | 163 | 163 | 163 |
| Retained Earnings | 162 | 177 | 216 | 238 | 266 | 301 |
| Other Reserves | 90 | 100 | 95 | 95 | 95 | 95 |
| Shareholders' Equity | 415 | 440 | 474 | 496 | 524 | 559 |
| Tier 1 Perpetual Notes | 116 | 116 | 167 | 167 | 167 | 167 |
| Total Equity & Liabilities | 3,633 | 4,081 | 4,294 | 4,727 | 5,097 | 5,483 |
| Cash Flow Statement | | | | | | |
| Cash from operations | (74) | 100 | (80) | 83 | (5) | 71 |
| Cash from investing activities | 2 | 3 | 3 | 8 | 9 | 10 |
| Cash from financing | (42) | (5) | 37 | (42) | (47) | (53) |
| Net changes in cash | (118) | 92 | (46) | 32 | (62) | 8 |
| Cash at the end of period | 216 | 308 | 262 | 294 | 232 | 241 |
| Key Ratios | | | | | | |
| Return on Average Assets | 0.5% | 0.8% | 1.2% | 1.4% | 1.5% | 1.7% |
| Return on Average Equity | 4.3% | 7.1% | 10.6% | 13.2% | 14.9% | 16.3% |
| Net Interest & Islamic Finance Income / Operating Income | 74.3% | 70.6% | 70.9% | 70.7% | 70.5% | 70.2% |
| Other operating income / Operating Income | 25.7% | 29.4% | 29.1% | 29.3% | 29.5% | 29.8% |
| Net fee Income/Operating Income | 11.1% | 15.3% | 14.9% | 16.0% | 17.6% | 19.7% |
| Interest Earning/Financing Assets Yield | 5.02% | 4.76% | 4.87% | 5.02% | 5.07% | 5.12% |
| Cost of Funds | -2.54% | -2.45% | -2.47% | -2.52% | -2.58% | -2.64% |
| Net Spread | 2.48% | 2.32% | 2.40% | 2.50% | 2.50% | 2.48% |
| Cost to Income Ratio | 54.6% | 51.5% | 43.8% | 39.6% | 36.9% | 34.8% |
| Net Loans & Islamic Financing to Customer Deposits (Total LTI) | 114.3% | 105.9% | 110.1% | 108.0% | 109.0% | 108.5% |
| NPLs to Gross Loans & Islamic financing | 5.6% | 5.3% | 5.6% | 5.6% | 5.7% | 5.7% |
| NPL Coverage, % | 92.3% | 88.4% | 80.8% | 82.8% | 84.7% | 86.6% |
| Cost of Risk, bps | 96.3 | 69.0 | 53.8 | 54.0 | 52.0 | 48.0 |
| Shareholders' Equity to Total Loans & Islamic Financing, x | 0.17 | 0.17 | 0.18 | 0.17 | 0.16 | 0.16 |
| Shareholders' Equity to Total Assets, x | 0.15 | 0.14 | 0.15 | 0.14 | 0.14 | 0.13 |
| Capital Adequacy Ratio, % | 16.4% | 15.8% | 16.9% | 16.0% | 15.3% | 15.0% |
| EPS, OMR | 0.011 | 0.019 | 0.030 | 0.039 | 0.047 | 0.054 |
| BVPS, OMR | 0.255 | 0.271 | 0.291 | 0.305 | 0.322 | 0.344 |
| Market Price, OMR* | 0.160 | 0.196 | 0.299 | 0.299 | 0.299 | 0.299 |
| Cash Dividend Payout Ratio, % | 0.0% | 19.9% | 35.0% | 45.0% | 45.0% | 45.0% |
| Cash Dividend Yield, % | 0.0% | 1.9% | 3.5% | 5.9% | 7.0% | 8.2% |
| P/E Ratio, x | 14.3 | 10.5 | 10.1 | 7.6 | 6.4 | 5.5 |
| P/BV Ratio, x | 0.6 | 0.7 | 1.0 | 1.0 | 0.9 | 0.9 |

* - Market price for current year and subsequent years as per the latest closing price.

Source: Company Financials, U Capital Research

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Oman Arab Bank

Recommendation: Accumulate
Target Price: 0.169
Upside/ (Downside): 13.6%

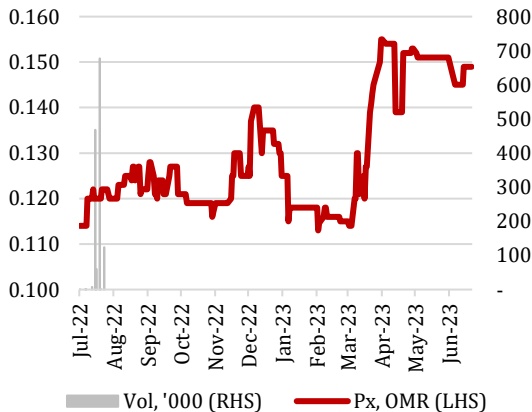
| | |
|------------------------------|-------------------|
| Recommendation | Accumulate |
| Bloomberg Ticker | OAB OM |
| Current Market Price (OMR) | 0.142 |
| 52wk High / Low (OMR) | 0.170/0.110 |
| 12m Average Vol. (000) | 119 |
| Mkt. Cap. (USD/OMR mn) | 616/237 |
| Shares Outstanding (mn) | 1,669 |
| 3m Avg Daily Turnover | 9.5 |
| 6m Avg Daily Turnover | 17.0 |
| P/E'23e (x) | 10.9 |
| P/B'23e (x) | 0.7 |
| Cash Dividend Yield '23e (%) | 2.8% |

Price Performance:

| | |
|--------------|----|
| 1 month (%) | -6 |
| 3 month (%) | -2 |
| 12 month (%) | 21 |

Source: Bloomberg

Price-Volume Performance



Source: Bloomberg

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- Spreads improving despite the bank's high dependence on costlier time deposits (c.49% of total deposits vs. peer average at 44%).
- Capital adequacy ratio at 16.2%, well-above the regulatory minimum; CET1 ratio lowest within sector at 10.2%.
- OAB's cost of risk is expected to have peaked in 2021 and we include tapering off of the cost of risk over the forecast period

We revise our rating on Oman Arab Bank to ACCUMULATE with a target price OMR 0.175 per share. The current price implies a P/E'23e and a P/B'23e of 10.6x and 0.7x respectively. We believe that this target price is justified because the worst is likely over for the bank in terms of heightened cost of risk and other issues.

Investment summary

We believe that OAB will be grow its net loans & Islamic financing at a CAGR of 6.5%. Furthermore, its operating income is expected to grow at a CAGR of 6.9% over the forecast period from growth in total interest & Islamic finance income. Its operating expenses are expected to increase at a higher pace than operating income. OAB's cost of risk is expected to have peaked in 2021 and we include tapering off of the cost of risk over the forecast period. We have been conservative in our estimates for the reduction in the cost of risk and we believe that if the bank is able to bring the cost of risk down at a faster pace, then this will provide further upside to our valuation.

2Q23 earnings summary

OAB's net profit rose 68%YoY to reach OMR 6.0mn for 2Q23. Net profit for 1H23 is at OMR 11.5mn, higher by 63%YoY. The recovery in profit is a result of an improvement in operating profit as well as a reduction in net ECL & tax charges. We estimate significantly lower ECL charges in the quarter (-23% YoY) by estimating a 15.5% tax rate for the quarter. The bank's operating expenses are lower by 4% for 1H23 and flat YoY for 2Q23 indicating tight cost control. Despite a 2%YoY decline in operating income for 1H23, decline in operating expense helped boost the operating profit by 2%YoY. On quarterly basis, op expenses increased 1%QoQ and flat YoY. The bank has restated its 1H22 op income and expenses numbers. The bank has posted a 12%YoY & 2%QoQ growth in its net loans & Islamic financing portfolio, in line with our estimate. Its customer deposits rose 11%YoY and 2%QoQ.

Key Indicators

| Year | FY20 | FY21 | FY22 | FY23e | FY24e | FY25e |
|----------------------------------|---------|---------|---------|---------|---------|---------|
| Total Net Loans (OMR mn) | 2,635.5 | 2,753.4 | 3,067.1 | 3,281.8 | 3,478.7 | 3,687.4 |
| Total Customer Deposits (OMR mn) | 2,755.3 | 2,810.4 | 2,992.2 | 3,342.8 | 3,539.8 | 3,748.4 |
| Operating Income (OMR mn) | 101.0 | 121.6 | 122.6 | 132.8 | 141.1 | 151.3 |
| Net Profit (OMR mn) | 14.2 | 7.1 | 16.2 | 22.8 | 28.7 | 35.4 |
| Diluted EPS (OMR) | 0.008 | 0.004 | 0.010 | 0.014 | 0.017 | 0.021 |
| Diluted BVPS (OMR) | 0.215 | 0.213 | 0.215 | 0.229 | 0.242 | 0.256 |
| P/E (x) | 22.4 | 37.7 | 16.5 | 10.9 | 8.7 | 7.0 |
| P/B (x) | 0.9 | 0.8 | 0.7 | 0.7 | 0.6 | 0.6 |
| Dividend Yield (%) | 0.0% | 0.0% | 0.0% | 2.8% | 4.5% | 5.7% |

Source: Company Financials, U Capital Research

Key Financials

| (OMR mn) | FY20 | FY21 | FY22 | FY23e | FY24e | FY25e |
|--|--------------|--------------|--------------|--------------|--------------|--------------|
| Income Statement | | | | | | |
| Interest/Financing Income | 143.6 | 166.6 | 178.6 | 195.0 | 217.6 | 242.8 |
| Interest Expense/Payment to Depositors | (63.5) | (77.0) | (78.5) | (87.0) | (99.0) | (111.2) |
| Net Interest/Financing Income | 80.1 | 89.5 | 100.2 | 108.0 | 118.6 | 131.6 |
| Fee & Commission Income | 15.5 | 17.2 | 17.8 | 19.7 | 21.3 | 22.9 |
| Other Income | 5.4 | 14.8 | 4.6 | 5.1 | 5.5 | 5.9 |
| Total Non-Interest/Financing Income | 31.0 | 53.3 | 48.1 | 52.5 | 56.1 | 60.2 |
| Total Operating Income | 101.0 | 121.6 | 122.6 | 132.8 | 141.1 | 151.3 |
| Operating Expenses | (65.4) | (78.5) | (74.8) | (77.0) | (80.5) | (84.7) |
| Operating Profit | 35.6 | 43.2 | 47.8 | 55.8 | 60.7 | 66.5 |
| Provisions expense | (17.7) | (35.2) | (30.3) | (31.2) | (29.8) | (28.3) |
| Profit Before Taxation | 17.9 | 8.0 | 17.5 | 24.6 | 30.9 | 38.2 |
| Taxation & others | (3.8) | (0.9) | (1.3) | (1.8) | (2.3) | (2.8) |
| Net Profit Attributable to Parent | 14.2 | 7.1 | 16.2 | 22.8 | 28.7 | 35.4 |
| Interest of Tier 1 Perpetual Securities | (5.5) | (10.2) | (9.2) | (9.2) | (9.2) | (9.2) |
| Net Profit Attributable to shareholders | 8.6 | (3.1) | 7.0 | 13.6 | 19.5 | 26.2 |
| Balance Sheet | | | | | | |
| Cash Balances | 221 | 189 | 100 | 248 | 251 | 256 |
| Deposits with Banks & FIs | 73 | 51 | 54 | 57 | 61 | 65 |
| <i>Gross Loans & Islamic financing</i> | <i>3,447</i> | <i>3,724</i> | <i>4,191</i> | <i>4,548</i> | <i>4,905</i> | <i>5,295</i> |
| <i>Loan Loss Reserve (Conventional + Islamic)</i> | <i>(104)</i> | <i>(141)</i> | <i>(180)</i> | <i>(192)</i> | <i>(204)</i> | <i>(216)</i> |
| Net Loans & Islamic financing | 3,342 | 3,583 | 4,011 | 4,356 | 4,701 | 5,079 |
| Investments | 240 | 302 | 332 | 355 | 376 | 399 |
| Net Fixed Assets | 47 | 43 | 38 | 39 | 40 | 41 |
| Other Assets | (623) | (733) | (853) | (977) | (1,120) | (1,283) |
| Total Assets | 3,300 | 3,436 | 3,682 | 4,078 | 4,309 | 4,555 |
| Deposits from Banks & FIs | 14 | 13 | 94 | 105 | 111 | 118 |
| Total Customer Deposits | 2,755 | 2,810 | 2,992 | 3,343 | 3,540 | 3,748 |
| Other Borrowings | 20 | - | - | - | - | - |
| Other Liabilities | 79 | 88 | 98 | 109 | 116 | 123 |
| Total liabilities | 2,868 | 2,911 | 3,184 | 3,557 | 3,767 | 3,989 |
| Paid-up Capital | 167 | 167 | 167 | 167 | 167 | 167 |
| Retained Earnings | 53 | 68 | 71 | 91 | 109 | 129 |
| Other Reserves | 139 | 121 | 121 | 124 | 127 | 131 |
| Shareholders' Equity | 359 | 356 | 359 | 382 | 403 | 428 |
| Minority Interest &/or Tier 1 Perpetual Notes | 73 | 169 | 139 | 139 | 139 | 139 |
| Total Equity & Liabilities | 3,300 | 3,436 | 3,682 | 4,078 | 4,309 | 4,555 |
| Cash Flow Statement | | | | | | |
| Cash from operations | (0) | (101) | (51) | 148 | 11 | 17 |
| Cash from investing activities | 7 | (3) | (5) | 1 | 1 | 1 |
| Cash from financing | 49 | 66 | (43) | 0 | (7) | (11) |
| Net changes in cash | 41 | (32) | (89) | 148 | 4 | 5 |
| Cash at the end of period | 221 | 189 | 100 | 248 | 251 | 256 |
| Key Ratios | | | | | | |
| Return on Average Assets | 0.5% | 0.2% | 0.5% | 0.6% | 0.7% | 0.8% |
| Return on Average Equity | 4.3% | 2.0% | 4.5% | 6.2% | 7.3% | 8.5% |
| Net Interest Income & Islamic Finance Income/ Operating Income | 79.3% | 73.6% | 81.7% | 81.3% | 81.0% | 81.0% |
| Other Operating Income/Operating Income | 20.7% | 26.4% | 18.3% | 18.7% | 19.0% | 19.0% |
| TangRoAE (after Interest on Tier 1 Perpetual Notes) | 2.7% | -0.9% | 2.0% | 3.7% | 5.1% | 6.4% |
| Interest Earning/Finance Asset Yield | 5.6% | 5.5% | 5.4% | 5.5% | 5.7% | 6.0% |
| Cost of Funds | 2.6% | 2.7% | 2.7% | 2.7% | 2.8% | 3.0% |
| Net Spread | 2.9% | 2.8% | 2.8% | 2.8% | 2.9% | 3.1% |
| Net Interest Margin (NIM), % | 3.1% | 3.0% | 3.1% | 3.0% | 3.1% | 3.3% |
| Cost to Income Ratio | 64.7% | 64.5% | 61.0% | 58.0% | 57.0% | 56.0% |
| Net Loans to Customer Deposits | 95.7% | 98.0% | 102.5% | 98.2% | 98.3% | 98.4% |
| NPLs to Gross Loans & Islamic Financing, % | 4.6% | 4.8% | 5.1% | 5.1% | 5.2% | 5.2% |
| NPL Coverage, % | 84.4% | 102.2% | 108.4% | 107.7% | 107.1% | 106.5% |
| Cost of Risk (bps) | 74.9 | 125.3 | 96.2 | 87.2 | 78.2 | 70.2 |
| Shareholders' Equity to Total Assets, x | 0.11 | 0.10 | 0.10 | 0.09 | 0.09 | 0.09 |
| Capital Adequacy Ratio, % | 15.1% | 17.7% | 17.0% | 17.3% | 16.9% | 16.6% |
| EPS (OMR) | 0.008 | 0.004 | 0.010 | 0.014 | 0.017 | 0.021 |
| BVPS (OMR) | 0.215 | 0.213 | 0.215 | 0.229 | 0.242 | 0.256 |
| Market Price (OMR) * | 0.190 | 0.160 | 0.160 | 0.149 | 0.149 | 0.149 |
| Cash Dividend Payout Ratio, % | 0.0% | 0.0% | 0.0% | 30.0% | 39.0% | 40.0% |
| Cash Dividend Yield, % | 0.0% | 0.0% | 0.0% | 2.8% | 4.5% | 5.7% |
| P/E Ratio (x) | 22.4 | 37.7 | 16.5 | 10.9 | 8.7 | 7.0 |
| P/BV Ratio (x) | 0.88 | 0.75 | 0.74 | 0.65 | 0.62 | 0.58 |
| P/TangBVPS | 0.90 | 0.77 | 0.76 | 0.7 | 0.6 | 0.6 |

*Market price for current year and subsequent years as per the closing price on 24-Jul-2023

Source: Bank Financials, U Capital Research

Sohar International Bank HSBC Bank Oman

Recommendation: Under Review
Target Price: Under Review
Upside/ (Downside): NA

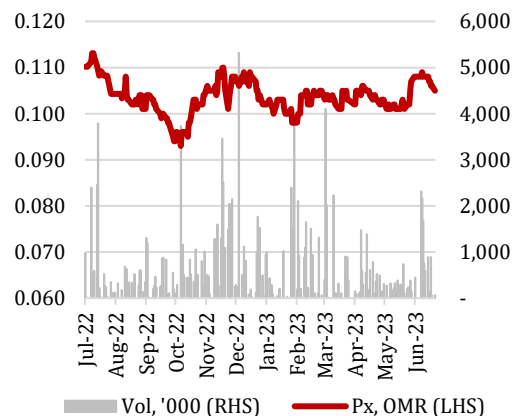
| Recommendation | Under Review |
|---------------------------------|--------------|
| Bloomberg Ticker | BKSB OM |
| Current Market Price (OMR) | 0.104 |
| 52wk High / Low (OMR) | 0.110/0.090 |
| 12m Average Vol. (000) | 547.8 |
| Mkt. Cap. (USD/OMR Mn) | 1,241/477 |
| Free Float (%) | 84% |
| 3m Avg Daily Turnover (OMR'000) | 44.3 |
| 6m Avg Daily Turnover (OMR'000) | 51.1 |
| P/E'22e (x) | 10.6 |
| P/B'22e (x) | 0.8 |
| Dividend Yield '23e (%) | 3% |

Price Performance:

| | |
|--------------|-----|
| 1 month (%) | 2.0 |
| 3 month (%) | 1.0 |
| 12 month (%) | 0.7 |

Source: Bloomberg

Price-Volume Performance



Source: Bloomberg

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- **BKSB is soon to become the second largest bank in Oman, post the merger with HSBC, due for completion in 2H23.**
- **Faster gross loan growth than sector (+11%YoY as of 1H23 ahead of peer-group average)**
- **Loan-to-deposit ratio stretched at 112.3%; one of the highest within peer group**
- **Provision cover stands at 91%, showing improvement YoY; NPL ratio stands at 4.9% as pf 1Q23**

We have placed BKSB on **Under Review**, as it currently under the process of merger with HSBC Bank Oman. The bank's core equity Tier 1 (CET1) ratio has been boosted through a 50% share capital increase through rights issue in 2022. For 2022, the bank's asset quality has declined and cost of risk for FY22 was reported at close to 103bps. We expect the cost of risks to reduce.

The merger between HSBC Oman and Sohar International Bank is expected to take place on Thursday 17 August. After this date, HSBC Oman will no longer exist, and all the customers will be transferred to Sohar International. We believe that the merger should be value accretive for BKSB shareholders, as HBMO has a stronger capital adequacy as compared to BKSB. Further, HBMO has a higher CASA ratio. Furthermore, since HBMO's cost-to-income ratio is higher than BKSB, BKSB can extract cost synergies from the merged entity. [Link](#) to our past report is here.

2Q23 earnings summary

The bank has posted 5%YoY growth, but a 22%QoQ decline in its net profit for 2Q23. Operating income was 14% below our estimate, increasing by 9%YoY although dropping 8%QoQ, while operating expenses rose 20%YoY and 3%QoQ, broadly in line with our estimate. Operating profit dropped 16%QoQ, landing 22% below our estimate. ECL charges declined 13% YoY to OMR 11.1m, which was below our estimate.

The bank's net loans & Islamic financing assets are up 11%YoY and Net loan-to-deposit ratio shot up to about 112.3% from 110.6% in 1Q23 and is above the 106.4% recorded a year ago due to higher growth reported in net loans compared to customer deposits in the quarter.

Key Indicators

| Year | FY20 | FY21 | FY22 | FY23e | FY24e | FY25e |
|----------------------------------|-------|-------|-------|-------|-------|-------|
| Total Net Loans (OMR mn) | 2,503 | 2,612 | 2,924 | 3,151 | 3,403 | 3,675 |
| Total Customer Deposits (OMR mn) | 2,232 | 2,394 | 2,560 | 2,771 | 3,006 | 3,260 |
| Operating Income (OMR mn) | 92 | 111 | 133 | 146 | 161 | 177 |
| Net Profit (OMR mn) | 20 | 28 | 35 | 44 | 51 | 59 |
| EPS (OMR) | 0.008 | 0.010 | 0.008 | 0.010 | 0.011 | 0.013 |
| BVPS (OMR) | 0.135 | 0.134 | 0.124 | 0.128 | 0.133 | 0.139 |
| P/E (x) | 11.2 | 11.9 | 14.9 | 10.6 | 9.1 | 7.9 |
| P/BVPS (x) | 0.67 | 0.85 | 0.92 | 0.80 | 0.78 | 0.74 |
| Dividend Yield (%) | 0.0% | 3.5% | 1.8% | 2.9% | 2.9% | 2.9% |

Source: Company Financials, U Capital Research

* Market price for current year and subsequent years as per latest closing price of 23-Jul-2023

Recommendation

| | |
|------------|-----------------------|
| BUY | Greater than 20% |
| ACCUMULATE | Between +10% and +20% |
| HOLD | Between +10% and -10% |
| REDUCE | Between -10% and -20% |
| SELL | Lower than -20% |

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