

National Bank of Abu Dhabi

Robust growth across all business segments

INVESTMENT RESEARCH

COMPANY UPDATE | April 29, 2008

UNITED ARAB EMIRATES

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Last Price: AED 20.5
Price Target: AED 25.8
Sector: Banks

Stock Rating
UNDERPRICED

BLOOMBERG: NBAD UH

REUTERS: NBAD.AD

Share Data

No of shares (m)	1,976.6
Daily vol (US\$m)	3.4
Daily vol (AEDm)	12.5
Free Float	29.5%
Mkt cap (US\$m)	11,041
Mkt cap (AEDm)	40,521

Source: Reuters

Core banking income remains strong

Net interest income was up by 43.9% YoY to AED 776.7m in Q1/08. Loan book grew by 16.4% QoQ and 51.1% YoY funded by core customer deposits, which increased by 12.8% QoQ and 28.9% YoY.

Exceptional item giving further fillip to non-interest income

The bank reported non-interest income of AED 509.0m, up by 69.9% YoY. This was on the back of one-off gain of AED 165m from the sale of land. Adjusted for this, the non-interest income grew by 14.8%. Fees and commission income increased by 21.3% YoY to AED 273.5m. In order to diversify and shore up its fee-based income stream, the bank has undertaken initiatives such as private banking, real estate and Islamic finance.

Solid fundamentals, attractive valuation

NBAD is better known as the bank of the Abu Dhabi Government. It has strong relationships with the Government and the public sector companies. In our view, the bank is well positioned to capitalize on the economic boom in the UAE in general and Abu Dhabi in particular. Thrust towards consumer lending is likely to give a further fillip to the overall loan book. The consistent growth in core business and initiatives towards new business lines should enable the bank to register robust earnings growth over the foreseeable future.

We have positively revised our estimates to reflect the solid Q1/08 results and incorporate the one-off gain on sale of land. We adjust our target price to AED 25.8 per share, a potential upside of 25.9% and 5.4% higher than our previous target price of AED 24.5. Our recommendation remains **Underpriced**.

Forecast and Ratios

Yr to Dec	Net int. income (AEDm)	Operating Income (AEDm)	Profit (AEDm)	EPS (AED)	PE (x)	Book value (AED)	PB (x)
2007	2,405.0	3,665.6	2,505.1	1.6	14.5	7.0	3.2
2008E	3,016.9	4,749.8	3,235.7	1.6	12.5	7.0	2.9
2009E	3,661.0	5,769.3	3,853.2	1.9	10.5	8.6	2.4
2010E	4,359.6	7,044.5	4,708.1	2.4	8.6	10.6	1.9
2011E	5,057.2	8,453.6	5,620.5	2.8	7.2	13.2	1.6

Source: TNI Investment Research

Stock price performance



Source: Reuters

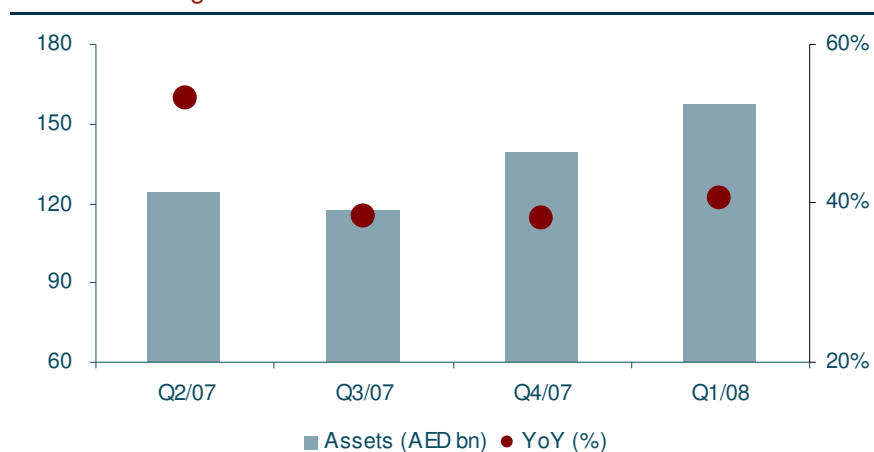
Analysis of Q1/08

Strong balance sheet expansion...

Total assets reached AED 157.2bn at the end of the first quarter of 2008, up by 12.8% QoQ and 40.5% YoY. The bank has reported sequential growth in overall assets in the last five quarters supported by a solid deposits franchise. The government's diversification programme involves a massive pipeline of planned infrastructure and development projects, a large portion of these projects are being undertaken in the Emirate of Abu Dhabi. As a result, net advances increased by 16.4% QoQ and 51.1% YoY to AED 92.8bn in Q1/08.

In our view, the demand for loanable funds is likely to remain strong over the foreseeable future on the back of the Government's thrust towards infrastructure spending, increasing private sector participation and a growing population requiring banking services. Going forward, we expect net loans to grow at a CAGR of 30.7% over the next four years.

Chart 1: Asset growth



Source: Company Reports, TNI Investment Research

Table 1: Select balance sheet indicators

	Q1/07	2007	Q1/08	% Growth (YoY)	% Growth (QoQ)	2008E	% Growth (YoY)
Loans and advances (net)	61,380.9	79,729.1	92,770.1	51.1%	16.4%	110,843.7	39.0%
Customer deposits	71,518.6	81,736.7	92,181.3	28.9%	12.8%	105,262.4	28.8%
Total assets	111,877.1	139,430.7	157,231.1	40.5%	12.8%	175,007.3	25.5%

Source: Company Reports, TNI Investment Research

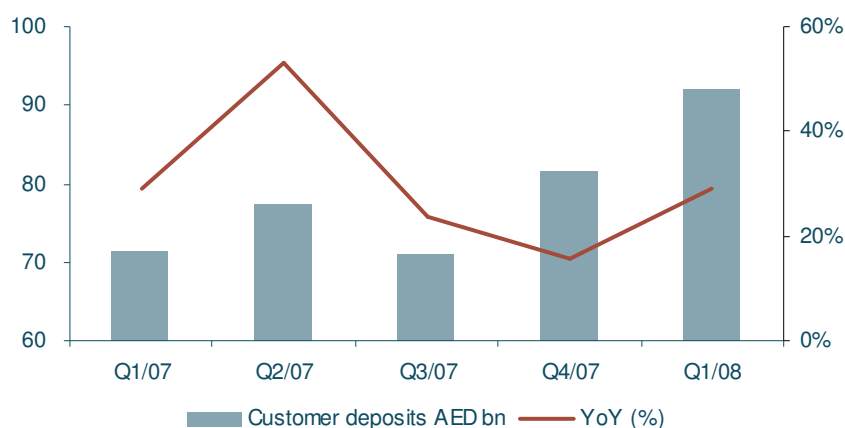
...on the back of robust funding base

Customer deposits were up by 12.8% QoQ and 28.9% YoY to AED 92.2bn in Q1/08. During the first quarter of 2008, the bank finalised the terms of an AED 2bn convertible bond issue. A part of the earlier convertible bond issued in 2006 was converted in Q1/08. For the year

Analysis of Q1/08

ended 2007, the bank issued stock dividend of 20%. As a result of the convertible bond issue and stock dividends for the year 2007, the issued share capital increased from AED 1.59bn in 2007 to AED 1.98bn in Q1/08. This will further support the strong demand for financing from both the corporate and consumer segments.

Chart 2: Deposit franchise

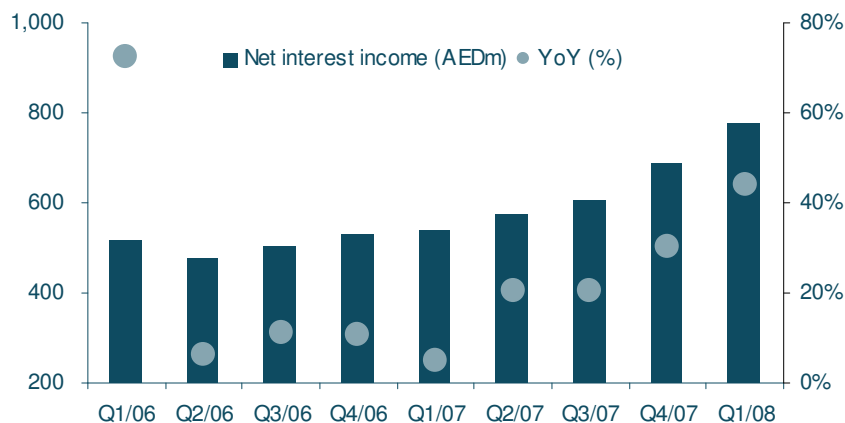


Source: Company Reports, TNI Investment Research

...resulting in core banking income growth

Net interest income was up by 43.9% YoY to AED 776.7m in Q1/08. For the first quarter of 2008, interest income grew by 11.8% YoY. However, interest expense declined by 4.7% YoY. In the last four quarters, core banking income growth YoY has been above 20%, and we expect this trend to continue over the foreseeable future due to the reasons cited before.

Chart 3: Core banking income



Source: Company Reports, TNI Investment Research

Analysis of Q1/08

Table 2: Key income statement parameters

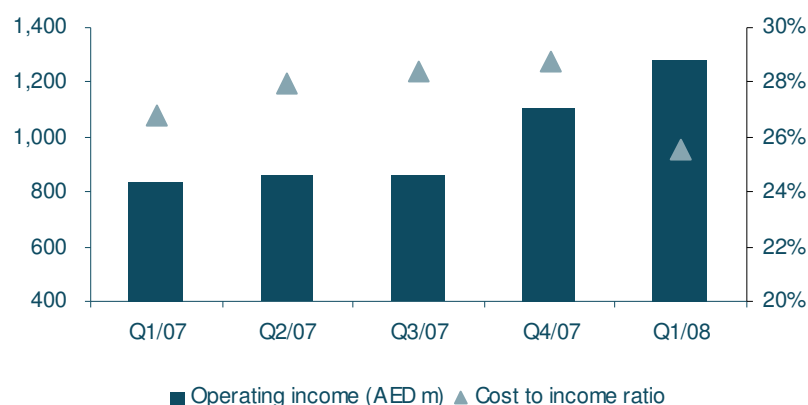
	Q1/07	2007	Q1/08	% Growth (YoY)	2008E	% achieved
Net interest income	539.6	2,405.0	776.7	43.9%	3,016.9	25.7%
Non-interest income	299.5	1,260.6	509.0	69.9%	1,732.9	29.4%
Operating income	839.1	3,665.6	1,285.6	53.2%	4,749.8	27.1%
Net Profit	601.3	2,505.1	874.5	45.4%	3,235.7	27.0%

Source: Company Reports, TNI Investment Research

Operating overheads under control

Operating income increased by 53.2% YoY to AED 1.3bn in Q1/08, while operating expenses increased by 45.8% during the same period. As a result, the cost to income ratio declined from 26.8% in Q1/07 to 25.5% in Q1/08, much below the bank's internal level of 35.0%.

Chart 4: Cost structure



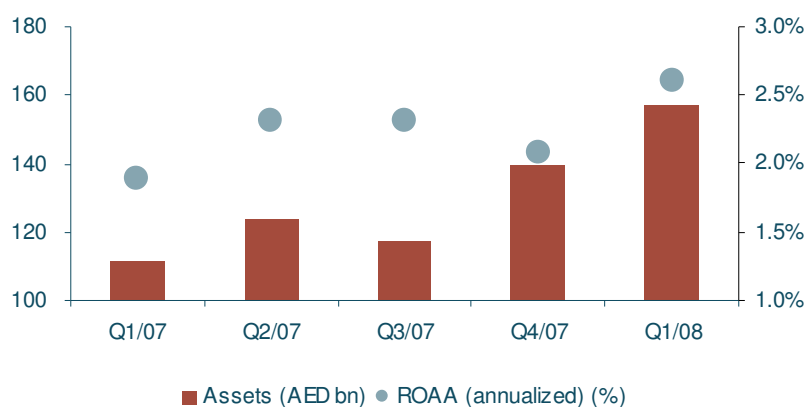
Source: Company Reports, TNI Investment Research

Improving return ratios

Net profit was up by 45.4% YoY to AED 874.5m in Q1/08. Both core banking income and non-interest income by way of one-off gain on property sale were the significant contributors to the strong growth in earnings. As a result, the return on average assets annualised (ROAA) increased from 1.9% in Q1/07 to 2.6% in Q1/08.

Analysis of Q1/08

Chart 5: Return ratios



Source: Company Reports, TNI Investment Research

Reported return on average equity (ROAE) in Q1/08 was 29.7%, higher than the bank's internal medium term target level of 25.0%. We have forecasted ROAE of 26.0%, 25.0%, 24.8% and 23.9% over the next four years.

The higher costs of funding and bargaining power of borrowers have resulted in margin compression during the last couple of years. This trend is likely to continue as competition in this sector intensifies further with the entrance of new players. However, we believe that the impact of margin contraction will not be significant as NBAD should offset by higher growth in volumes. We believe that earning should moderate over the next four years and hence expect a marginal decline in ROAE over the forecasted period.

Valuation

Revised estimates

We have revised our estimates to reflect the robust Q1/08 performance. During the same period, the bank finalised the terms of an AED 2bn convertible bond issue. A part of the earlier convertible bond issued in 2006 was converted in Q1/08. For the year ended 2007, the bank issued stock dividend of 20%. As a result of the convertible bond issue and stock dividends for 2007, the issued share capital increased from AED 1.59bn in 2007 to AED 1.98bn in Q1/08. We have increased our estimates for non-interest to reflect the one-off gain on sale of land in Q1/08, which we believe to be non-recurring in nature.

Table 3: New estimates

	Old estimates	New estimates	Deviation (%)
Loans and advances (net)	104,110.1	109,875.7	5.5%
Customer deposits	98,745.8	105,262.4	6.6%
Total assets	167,669.7	175,007.3	4.4%
Net interest income	2,907.4	3,016.9	3.8%
Non-interest income	1,542.2	1,732.9	12.4%
Operating income	4,449.6	4,749.8	6.7%
Net Profit	3,015.9	3,235.7	7.3%

Source: TNI Investment Research

Solid fundamentals, attractive valuation

At the current market price of AED 20.8, the stock is trading at 12.5x 2008E and 10.5x 2009E earnings. On a PB multiple, the stock is trading at 2.9x 2008E and 2.4x 2009E. Based on our valuation methodology and incorporating the robust Q1/08 performance, we arrive at a revised target price of AED 25.8 per share, an upside of 25.9% from the last closing price.

On our revised target price, NBAD would trade at an implied PB multiple of 3.7x 2008E and 3.0x 2009E and at an implied PE multiple of 15.8x 2008E and 13.2x 2009E. We believe premium valuations are justified on the back of the supportive macroeconomic environment, strong bank fundamentals and comfortable capital ratios to support growth in risk-adjusted assets and above industry return ratios.

Financial summary

Table 4: Financial highlights

AEDm	2007	2008E	2009E	2010E	2011E
Income statements					
Net interest income	2,405.0	3,016.9	3,661.0	4,359.6	5,057.2
Non-interest income	1,260.6	1,732.9	2,108.3	2,684.9	3,396.5
Operating expenses	1,054.4	1,373.3	1,741.7	2,119.1	2,566.7
Net Income	2,505.1	3,235.7	3,853.2	4,708.1	5,620.5
Balance sheets					
Net loans and advances	79,729.1	109,875.7	143,694.9	183,824.4	232,842.9
Customer deposits	81,736.7	105,262.4	133,689.5	168,146.4	209,445.7
Med & long term borrowing	9,950.7	14,225.0	17,898.0	19,734.5	21,571.0
Shareholders equity	11,214.2	13,809.2	16,998.8	21,042.8	25,998.7
Total assets	139,430.7	175,007.3	216,244.2	262,899.8	317,586.5
Cash flow statements					
Operating Cash Flow	(5,769.0)	3,845.9	3,982.6	4,812.2	3,857.8
Investing Cash Flow	335.9	(2,305.8)	(2,785.1)	(2,997.8)	(3,384.9)
Financing Cash Flow	3,544.4	3,637.7	3,014.1	1,177.6	1,177.6
Net Cash Flow	24,458.3	5,699.3	9,910.9	12,903.0	14,553.6
Ratios					
Return ratios					
ROAA	2.1%	2.1%	2.0%	2.0%	1.9%
ROAE	25.1%	26.0%	25.0%	24.8%	23.9%
Credit Quality					
NPLs to gross loans	1.1%	0.8%	0.7%	0.6%	0.5%
Loan Loss Reserve to Gross Loans	1.1%	0.9%	0.7%	0.6%	0.5%
NPL Coverage	106.0%	108.0%	109.7%	111.3%	113.0%
Margins					
Yield on interest earnings assets	6.3%	6.1%	6.2%	6.3%	6.4%
Cost on interest bearing liabilities	4.4%	4.2%	4.3%	4.5%	4.6%
Net interest margin	2.2%	2.1%	2.0%	2.0%	1.9%
Valuation					
EPS (AED)	1.6	1.6	1.9	2.4	2.8
BVPS (AED)	7.0	7.0	8.6	10.6	13.2
PE (x)	14.5	12.5	10.5	8.6	7.2
PB (x)	3.2	2.9	2.4	1.9	1.6

Source: Annual Report, TNI Investment Research

Financial summary

This report is solely intended to be a market update for the recipients of this report on certain information about the company, which we reasonably believe may be price sensitive. However it should be noted that the report does not constitute a recommendation or opinion expressed by TNI Investment Research, nor should be construed as a solicitation or offer, to buy or sell any securities. The content of the report should be read in conjunction with our initiation report on the company and disclaimers included therein.