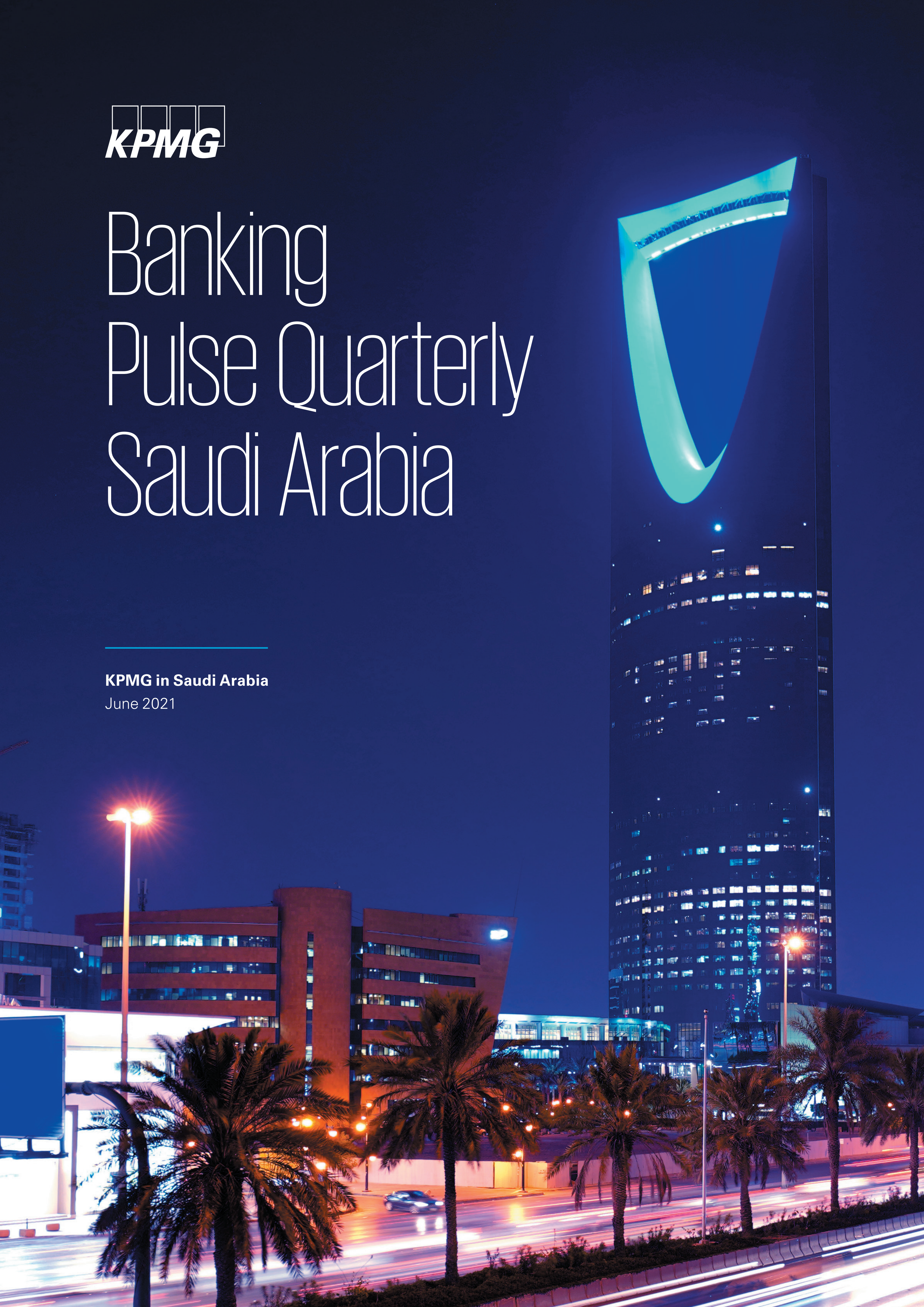
KPMG

Banking Pulse Quarterly Saudi Arabia

KPMG in Saudi Arabia

June 2021



Industry overview

For years, social psychologists have studied whether we can, and actually do, 'grow from adversity' – and we believe this is something that the financial services sector in Saudi Arabia has impressively demonstrated in recent times. More than a full year since the Covid-19 was officially declared as pandemic by the WHO, some of the performance developments in the Kingdom's banking industry are better than ever. With the sector's total assets - excluding Saudi Central Bank (SAMA) - crossing the SAR 3 trillion mark and total deposits approaching the SAR 2 trillion mark, the overall financial health of the system appears to be in great shape. Adding to that the phenomenal increase of over 30% in total credit since FY 2018, this speaks volumes of how well the sector has not only weathered the various recent challenges, but also is a testament of the profound positive impacts of Vision 2020 Financial Services Sector Development Program (FSDP) and the ensuing initiatives by SAMA.

From a pure financial performance perspective, the gradual decline in credit losses and strong growth in loan books have translated into 20% growth in average net income across the sector relative to Q1 2020. As noted previously as well, the reduction in credit losses of approximately 19% is a courtesy of the various measures taken by both the government as well as individual baking entities over the course of last year. These include, but are not limited to, the MSME support program (especially payment holidays), liquidity support to commercial banks as well as, careful underwriting and the exercise of enhanced credit diligence by banks. Another positive indicator for the sector is the maintenance of average coverage ratio above 169%, which, together with the average capital adequacy ratio of 21% (compared to 19% in Q1 2020), is a good reflection of sectors' shock absorption capacity.

However, amidst the positive performance indicators across various fronts, perhaps the most stellar of the lot is the monumental growth in real estate finance over the last two years. With an astounding increase of approximately 100% since FY 2018, the total financing on this front is fast approaching the SAR 500 billion mark. In fact, statistics reveal that the number of new residential mortgage contracts being written have grown almost ten times over the last three years to about 300,000. While this bodes very well for the housing sector, house ownership levels and wider economy, banks yet need to continue to exercise careful monitoring at both credit risk and asset-liability committee (ALCO) fronts, given the susceptibility of this asset class to market prices and the relatively longer maturities.

Moreover, from a qualitative perspective, the completion of the merger between NCB and SAMBA into the Saudi National Bank (SNB), just after the turn of the first quarter, marked the culmination of a much-anticipated milestone. The merger holds both historic and symbolic significance, not just for the banking sector, but overall Saudi economy. This event, followed by the recent mergers at SAAB and FAB, is a confirmation that M&A activity within banking is well and truly on track in the GCC region. With an expected post-merger total asset and total deposit book of SAR 880 billion and SAR 616 billion respectively, the Saudi National Bank is expected to far exceed the average sector asset and deposit levels by 248% and 241% respectively.

In lieu of the growing banking penetration levels across the country, rapid developments across aspects such as digitization and ESG, as well as rising inoculation rates; the recent mergers continue to mount pressure on peer banks, not only from growth perspective but also in terms of the sustainability of current market share while maintaining healthy margins. In either case, the tides seem to be turning for the good and the sector's 'growth despite great adversity' is stronger than ever.

We wish you an insightful read of the next edition of our Banking Pulse which is part of a series of our industry-wide endeavor to share and seek insights in the banking space. We wish you all a good read and look forward to your feedback.

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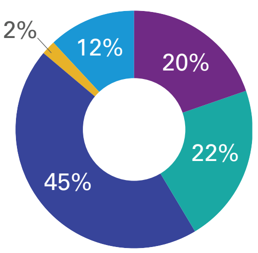
KPMG 2021 CEO Outlook Pulse Survey: Banking sector

A survey of 60 bank CEOs in 10 key markets, our 2021 Pulse Survey provides a timely snapshot of CEOs' views on business growth resumption, their views on vaccine distribution, their top-of-mind organizational risks, and business transformation priorities going forward.

Pandemic response

When do CEOs envision that their company will return to a normal course of business?



9 Out of 10 CEOs are keen to ensure **staff safety** by asking employees to notify the business when they have been **vaccinated**.

1/2 of bank leaders are concerned not all employees will have access to a **Covid-19 vaccine,** jeopardizing their operations and competitive advantage.

What do bank CEOs think it will take to return to 'normal'

A **successful Covid-19 vaccine roll-out** (at least 50% vaccinated)

Governments in key markets encouraging business to return to 'normal'

A significant **drop in Covid-19 infection** rates in key markets

Perspectives from banking leaders

Economic confidence

56% of bank CEOs have an appetite for **M&A.**

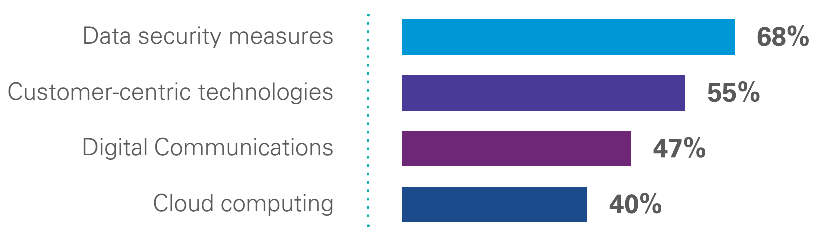
Top drivers for investment

1. On-board new **digital technology** to transform the **customer experience/value proposition**
2. Increase **market share**
3. **Transform** our business model **faster than organic growth** will deliver

Source: KPMG 2021 CEO Outlook Pulse Survey

Digital acceleration priorities

CEOs are planning to invest more in technologies such as:



Customer and technology are key focus areas for banks.

Long-term impact of the pandemic on banks

75%

Increased **the creation of new digital business models** and **revenue streams** by a matter of months (up from 52 percent in August 2020).

73%

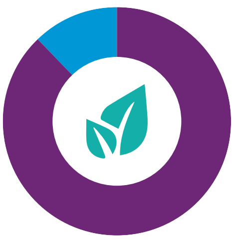
Believe **customer engagement** will be done predominantly via **virtual platforms.**

53%

Will build on the use of **digital collaboration** and **communications tools.**

Trust and reputation

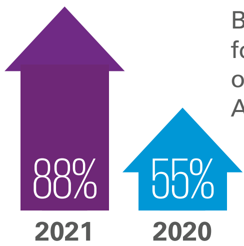
Continued focus on environment and climate risk



88%

Of bank CEOs are looking to lock in the **sustainability** and **climate** change gains made during the crisis.

Heightened focus on "S" component of ESG



Bank leaders are shifting their focus to the **social** component of their ESG program up from August 2020.

Top Diversity, Equity and Inclusion (DEI) and workforce agenda issues for bank CEOs

62%

Of bank leaders believe progress has moved **too slowly** on **diversity and inclusion.**

85%

Agree there is still much to do to build **gender diversity** on boards.

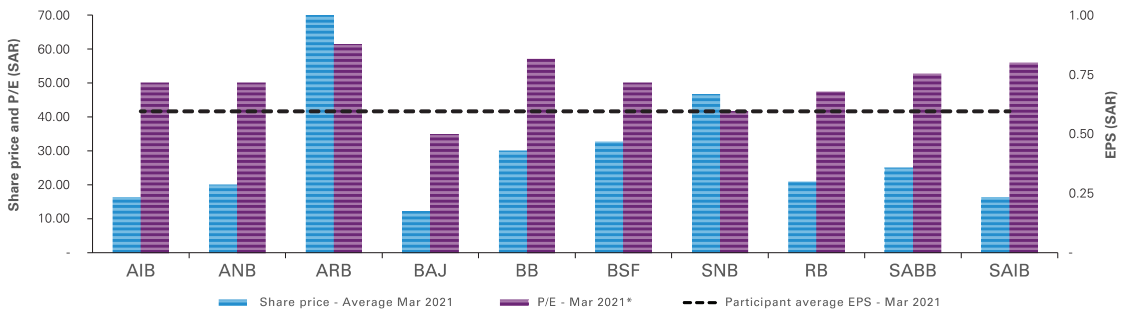
63%

will be increasing HR resources to **managing employee well** being and **mental health.**

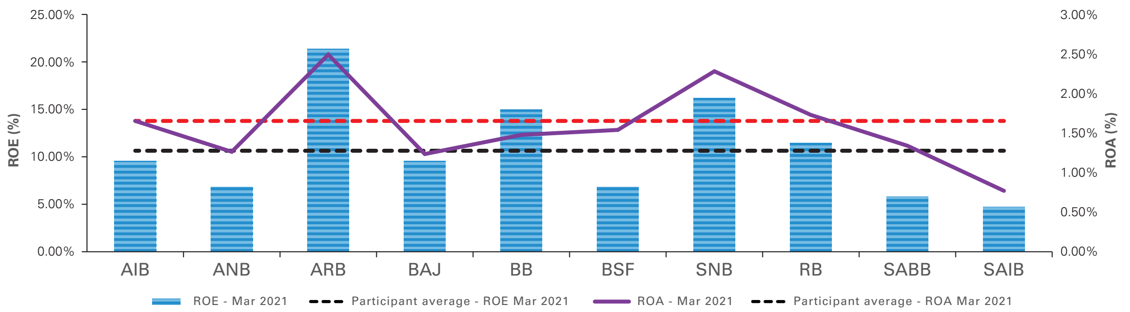
Source: KPMG 2021 CEO Outlook Pulse Survey

Q1 2021 financial performance of 10 listed banks in Saudi Arabia

Share price, P/E & EPS

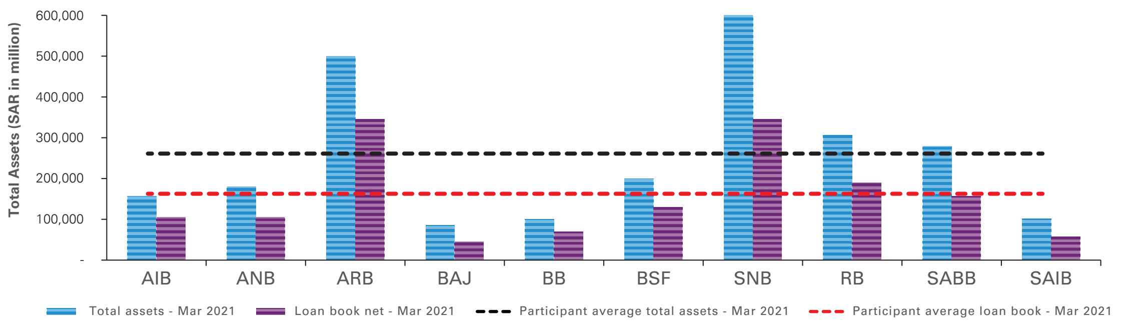


ROE & ROA



Net income

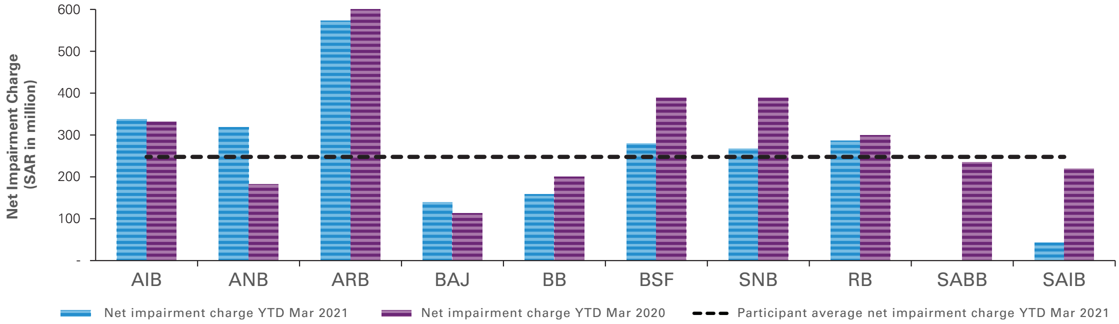
Total assets & Total loan book



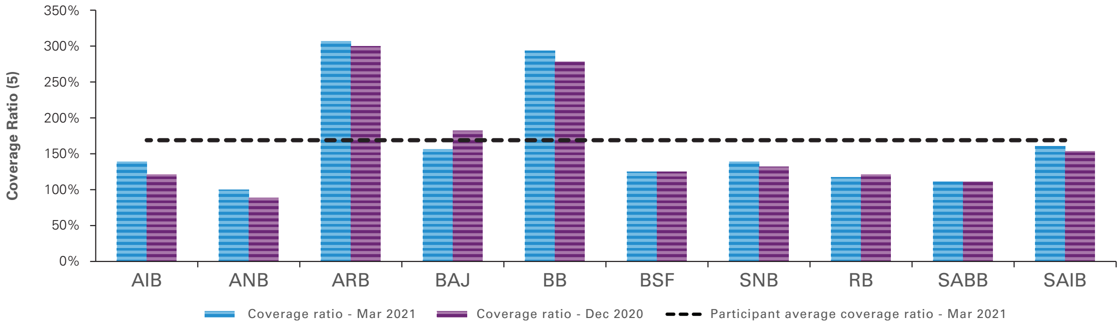
Legend:

Alinma Bank	**AIB**	Bank Al Bilad	**BB**	Saudi Investment Bank	**SAIB**
Arab National Bank	**ANB**	Banque Saudi Fransi	**BSF**	Saudi National Bank	**SNB**
Al Rajhi Bank	**ARB**	Riyad Bank	**RB**		
Bank Al Jazira	**BAJ**	Saudi British Bank	**SABB**		

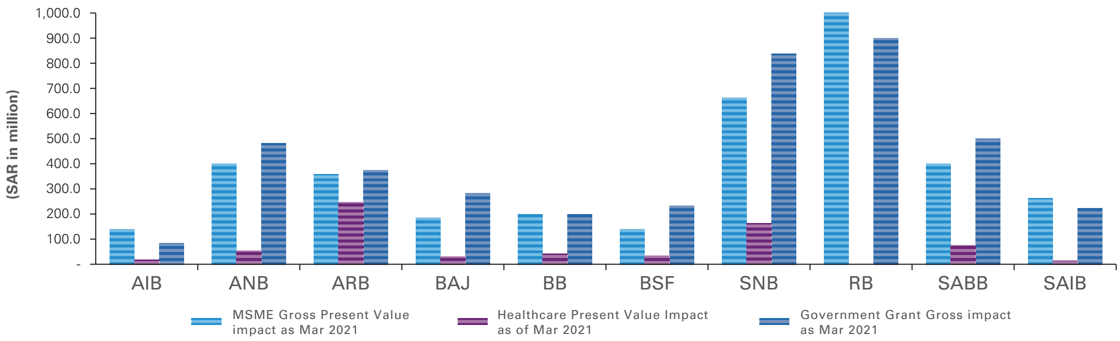
Net impairment charge



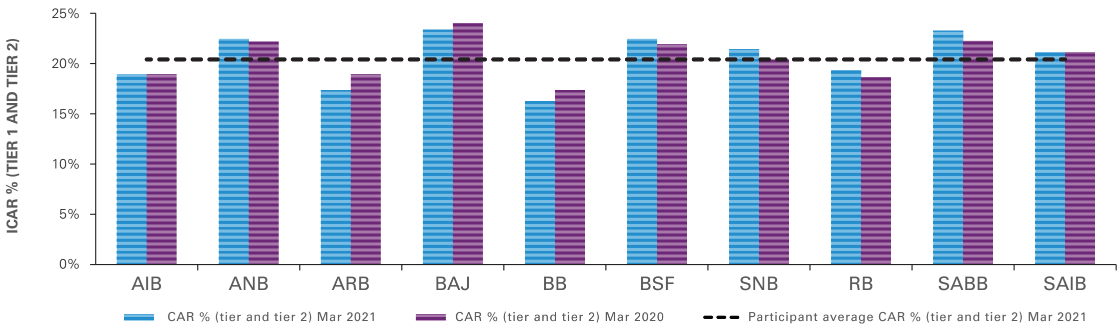
NPL coverage ratio



Impact driven by Covid-19



Capital adequacy ratio



Glossary:

P/E ratio is calculated as the average closing price (as derived from Tadawul) divided by the earnings per share (EPS). **ROE** is the ratio of net income for the period ended 31 March 2021 prorated to full year to total equity. **ROA** is the ratio of net income for the period ended 31 March 2021 prorated to full year to total assets. **Interest margin** is the ratio of net special commission income to total special commission income. **Coverage ratio** is the ratio of total ECL for loans and advances to total NPL. **Loan to deposit ratio** is the ratio of total loans and advances to total deposits.

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