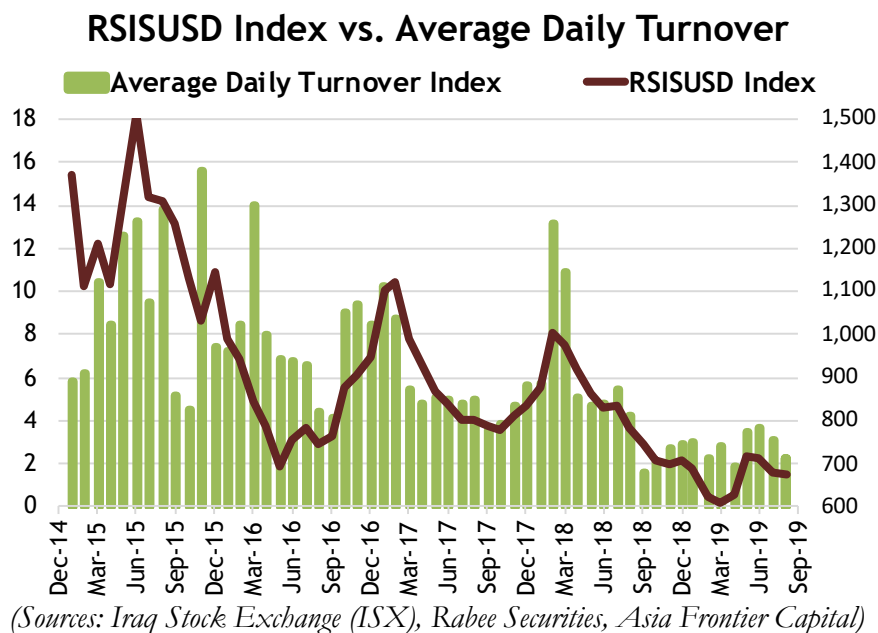


## Market Review: “Life returns to the banks”

Ahmed Tabaqchali, September 8<sup>th</sup>, 2019

The market drifted lower in an Eid-holiday shortened month, as turnover declined substantially from July. However, life found its way back to the banks. For the month, the market, as measured by the Rabee Securities RSISX USD Index (RSISUSD), was down  $-0.95\%$  and down  $-4.89\%$  for the year.

Average daily turnover declined  $-40\%$  month-month and was the third lowest level over the last five years- the others being April 2019 and September 2018 as can be seen from the chart below. Foreign investors continued to be net buyers, consistent with the trend of the last few months, although at lower total levels in-line with the decline in total turnover.



The market’s dynamics continue to improve with the return of life to the banking sector, which as a group cooled-off over June and July after a powerful rally in May led by the Bank of Baghdad (BBOB). This month, the group was led by the National Bank of Iraq (BNOI), which was up  $+21.1\%$  for the month and up  $+58.6\%$  from the April close before the sector started its rally. Moreover, its earnings report for the second quarter 2019 (Q2/2019) supported management’s bullish outlook for 2019 as expressed in its latest AGM. As reported here, in June’s update, while management decided not to distribute dividends for a challenging 2018, it indicated the possibility of resuming dividend payments for 2019 based on its strong results for the first half of the year, as well as positive expectations for the second half. BNOI’s first half 2019 (H1/2019) results show customer deposits were up  $+28\%$  year to date, while its loan book was up  $+77\%$  for the same period. Pre-tax earnings for the second quarter were up  $+48\%$  sequentially, with the year to date figure showing promise for the year - a long way to go before recovering to pre-crisis levels- but supporting management’s expectations for the resumption of dividend payments for 2019’s earnings.

While it’s not possible to extrapolate much from these results, or to generalize for the sector from them, they support in any case the thesis, made here in the last few months, which argues that the conditions are in place for the sector’s recovery in 2019-2020. The Commercial Bank of Iraq’s (BCOI) Q2/2019 earnings, while supporting this thesis, nevertheless show the unevenness of these conditions given the different circumstances of each bank. BCOI’s consumer deposits in H1/2019 were up  $+6\%$  year to date, while its loan book declined by  $-7\%$  - however, BCOI’s loan book is insignificant at under 8% of its deposits. BCOI was up  $+4.4\%$  for the month and up  $+17.5\%$  from the April close before the sector started its rally.

The most interesting development for the sector during the month was the trading action in the Bank of Baghdad (BBOB), which at some stage was up +10.7%, before trimming most of these gains, to end up +3.6%. This comes on the back of its four-month wild ride, during which it rallied +62.5% in May, declined -12.8% in June, declined a further -17.6% in July, to end in August up +20.8% from the pre-rally close. The stock's ride started on speculative hopes that BBOB would resume dividend payments for its 2018 results, sputtered as BBOB poured cold water over these speculative hopes during its recent AGM, but seems to still have plenty of fuel left. This could imply that the market is looking past the bank's difficulties and focusing, instead, on the prospects of a bank following through with the recovery in its fortunes that began in 2018 as part of the overall conditions in place for the sector's future revival.

The market's looking past the weaknesses of BBOB is a further positive aspect of its improving dynamics as pointed here last month "*While, BBOB pulled the other leading banks up with it in May, it did not drag them lower in June and July which is very different than the market's responses to such disappointments in 2018. That time all banks were painted by the same brush, which shows a market that has begun to discriminate showing it has likely bottomed or is making a bottom.*" The year to date chart below for four leading banks shows these very different responses.

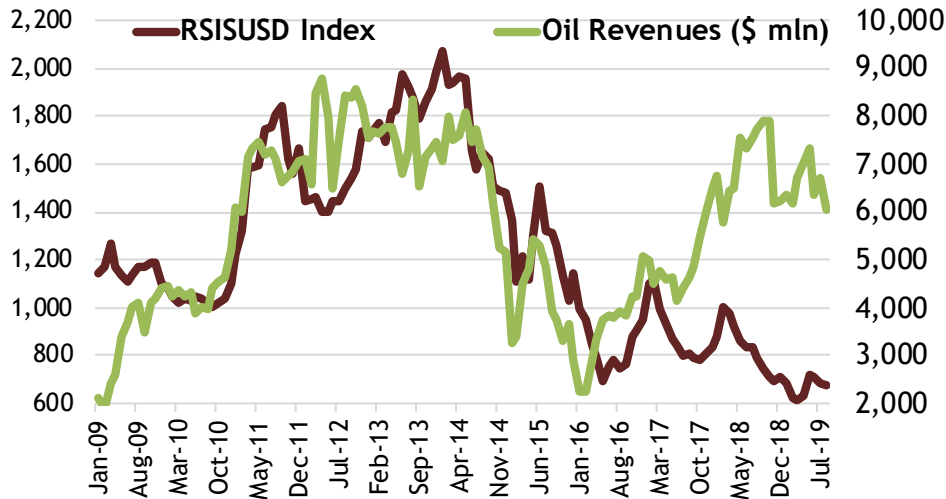
**Year to date indexed performance: Bank of Baghdad - BBOB (green), Commercial Bank of Iraq – BCOI (blue), Mansour Bank – BMNS (mauve), National Bank of Iraq - BNOI (brown)**



(Source: Bloomberg)

The early picture of the trading activity in September suggests that it will likely be in-line with that of August. Whilst the market is in the early process of discounting the banking sector's recovery, it's worthwhile to point out its continued divergence from its past close relationship with oil revenues (a proxy for the forces driving the economy) - still at the widest it has been for the last few years (see below).

## Oil Revenues vs. RSISUSD Index



(Sources: Iraq's Ministry of Oil, Rabee Securities, Asia Frontier Capital)  
 (Note: Oil revenues as of Jul, AFC estimates for Aug)

*Disclaimer*

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