



Equity Research - Initiation of Coverage

Sector: Banking

Country: Jordan

Date: August 28, 2012

Share Price (JOD): 7.99

Fair Value (JOD): 8.96

Upside: 12.2%

Recommendation: ACCUMULATE

Risk: Medium (Market)

Initiating coverage with a **ACCUMULATE** rating and a Fair Value of JOD 8.96 per share based on the analysis below**Expected double digit growth in earnings on lower provisions**

Earnings for 2011 grew by 13% to USD305 million, rebounding after steep declines of 53% and 35% during the preceding two years. This expansion was attributed to increases in both interest and commissions, along with a decrease in the amount of provisions taken. We estimate this growth to be sustained, with 2012 profits set to increase by 20%. Arab Bank's provisions equaled an unacceptable 50% of pre-tax income during 2010 and 2011. This has had devastating effects on overall profits, and we expect these levels to normalize going forward.

Non-Performing loans decline as operating environment stabilizes

Improvement in credit quality was registered during 2011, signaling more favorable business conditions than the previous two years. Arab Bank's aggressive expansionary strategy has shielded the bank from country specific risk, but has also exposed it to some of the turbulence certain nations are currently experiencing. Watch-list loans as a percentage of total loans remained stable around 2.5%, with non-performing loans declining from 7.7% in 2010 to 7.0%.

Loans and customer deposits expected to grow but at a slower pace

Total loans for 2011 remained unchanged, with personal and retail loans representing the only growing segment, expanding by over 9% Y-o-Y. On the other hand, exposure to the government and public sector contracted by nearly 15% during the year. In our forecasts, we are expecting loans to grow at a conservative CAGR of around 6.0% between 2012-2015, compared to 9.0% registered during the last five years. As for customer deposits, we estimate growth at a CAGR of 6.3% between 2012 and 2015, compared to 8.0% over the last five years.

Chairman resignation and provision uncertainty keeps investors wary

We valued Arab Bank's share price at JOD 8.96 using a Dividend Discount Model based on a 5-year forecast using a WACC of 12.7% and a terminal growth rate of 5.0%. Nonetheless, the recent resignation of Chairman Shoman may negatively impact share performance in the short term. This took place after a months-long dispute with CEO Al-Sabbagh resulting in the appointment of new chairman Sabih Al-Masri. Along with the provision uncertainty that persists, this has led to a decline in the stock price leaving the bank relatively undervalued when comparing its P/B and P/CF ratios to competitors. The bank's P/E ratio however is significantly higher than the regional average due to its high provisions. We believe the share price has room to appreciate and may become an attractive opportunity as regional uncertainty subsides.

Share Data

Bloomberg Symbol	ARBK.JR
Reuters Symbol	ARBK.AM
Market Cap (JODm)	4,251
Number of Shares (m)	534
Free Float	46.0%
Price-to-Earnings 11	20.78
Price-to-Book 11	0.77

Share Performance



1 Month Return	13.1%
3 Month Return	7.00%
6 Month Return	10.4%
12 Month Return	-6.50%
52 Week Range	6.68 – 8.75

Performance and Forecasts

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(USD millions)	2010	2011	2012e	2013f	2014f	2015f
Net Interest Income	933	957	995	1,042	1,122	1,213
Net Income	271	306	370	438	535	634
EPS (USD)	0.47	0.55	0.66	0.78	0.95	1.13
BVPS (USD)	14.32	14.01	14.59	15.50	16.67	18.09
ROA (%)	0.60	0.67	0.77	0.87	0.99	1.10
ROE (%)	3.54	4.09	4.75	5.29	6.00	6.60

FINANCIALS & VALUATION

Year	2010	2011	2012e	2013f	2014f	2015f		
Earnings Summary								
Net Interest Income (USDm)	933	957	995	1,042	1,122	1,213		
Growth (%)	-11.0	2.5	4.0	4.8	7.6	8.1		
Net Fees and Commissions Income (USDm)	287	303	326	345	366	391		
Growth (%)	1.4	5.9	7.6	5.7	6.2	6.6		
Net Profit (USDm)	271	306	370	438	535	634		
Profit Margin (%)	13.3	15.0	17.0	18.4	20.4	21.9		
Net Profit Growth (%)	-53.0	13.0	20.9	18.5	22.0	18.5		
Earnings Per Share (USD)	0.47	0.55	0.66	0.78	0.95	1.13		
Price-to-Earnings (Forward P/E)	24.2	20.8	17.3	14.6	11.9	10.1		
Key Performance Indicators								
Yield on Assets (%)	3.8	3.9	3.9	4.0	4.2	4.4		
Cost of Liabilities (%)	1.7	1.8	1.8	2.0	2.2	2.4		
Spread (%)	2.1	2.1	2.1	2.0	2.0	2.0		
Customer Deposits (USDm)	27,455	28,745	30,182	31,993	34,072	36,457		
Growth (%)	-12.8	4.7	5.0	6.0	6.5	7.0		
Net Loans / Customer Deposits	77.8	72.9	73.6	73.4	73.2	73.0		
Net Loans (USDm)	21,347	20,955	22,222	23,497	24,949	26,601		
Growth (%)	-3.1	-1.8	6.0	5.7	6.2	6.6		
Book Value Per Share (USD)	14.32	14.01	14.59	15.50	16.67	18.09		
Asset Quality								
Non-Performing Loans (NPL) / Loans (%)	7.7	7.0	6.0	5.2	4.5	3.8		
Provisions / Loans (%)	2.2	2.1	1.8	1.6	1.3	1.0		
Profitability								
ROA (%)	0.6	0.7	0.8	0.9	1.0	1.1		
Gearing (Assets/Equity)	6.0	6.1	6.1	6.1	6.0	5.9		
ROE (%)	3.5	4.0	4.6	5.1	5.8	6.4		
Comparables								
	Valuation			Capital Structure (%)		Profitability (%)		
	P/E	P/BV	P/CF	Eq/As	Ln/Dp	Pv %	ROE	ROA
ARBK	20.8	0.77	5.65	16.80	78.50	1.93	4.00	0.67
MENA Average	11.8	1.34	11.1	14.50	85.80	1.01	12.37	1.63
Valuation								
In JODm	2012e	2013f	2014f	2015f	2016f	2017f		
Net Income (Att. to Shareholders)	250	296	361	427	498	578		
Payout Ratio (%)	53.5	54.2	44.4	43.7	37.5	36.9		
Dividends	133.5	160.2	160.2	186.9	186.9	213.6		
PV of Terminal Value	4,019							
PV of Dividends & Terminal Value	4,153	142.2	126.2	130.6	115.9	117.6		
Estimated Fair Value (Sum of PV)	4,785							
Outstanding Shares (in millions)	534							
Dividend per Share (in JOD)	0.25	0.30	0.30	0.35	0.35	0.40		
Growth (%)	0.00	20.0	0.00	16.7	0.00	14.3		
Share Value (JOD)								8.96

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INVESTMENT SUMMARY

We are initiating an ACCUMULATE rating on Arab Bank (ARBK) after carefully analyzing the following.

Macro-Economic Environment

Arab Bank's aggressive expansionary strategy has shielded the bank from country specific risk, but has also exposed it to some of the turbulence certain nations are currently experiencing. Saudi Arabia, which through Arab National Bank is the largest one country exposure, remains very promising as government spending and strong consumer demand are projected to sustain healthy growth levels. Jordan however, is currently undergoing political reforms along with proposed austerity measures. It is important that inflation be kept in check, as economic instability can quickly disrupt that current growth within the banking sector.

The Palestinian territories are projected to maintain their double digit growth in the near future. This expansion though must be understood within the context of the prevalent situation, as conditions are bleak, with per capita GDP being second lowest in the Middle East only ahead of Yemen. Very high unemployment and political instability remain major risks.

Presence in Africa carries great potential, but the constant political insecurity remains a major road block to long term growth. As for Europe, the proposed austerity measures, along with the possible civil unrest that it could lead to, brings a volatile environment that can be beneficial for solid and safe institutions.

Loan Portfolio

Arab Bank's direct credit facilities reveal a highly diversified loans portfolio with exposure to an array of sectors and geographic regions. These loans have been focused towards a mix of borrowers, with the main emphasis being on corporates. In 2011, large corporations accounted for 65% of the loans portfolio, with small and medium companies making up another 12%. Credit directed towards retail customers accounted for only 15%, but was the fastest growing category, expanding by 9% y-o-y.

Geographic diversity among loans issued was also evident, with Jordan receiving only 24% of the credit handed out. Other Arab countries, where the majority of the Arab Bank branches are located, accounted for 52% of the loans originated. Among the corporate loans, ARBK's exposure was diversified among all economic sectors. Industry & Mining had the largest share at 20.7% of total loans, with prominent presence within both the Trade and General Services sectors, making up 16.0% and 12.9% respectively.

Credit Quality

Credit quality at Arab Bank saw slight improvements in 2011, signaling a reversal in the worsening conditions of the previous two years. Watch-list loans (which are loans that may become non-performing) remained stable as a percentage of total loans at around 2.5%, with non-performing loans improving from a high of 8.3% in 2009 down to 7.0% in 2011. In absolute terms, non-performing loans have been steadily declining at around 9% per year since peaking in 2009. The majority of those loans along with the provisions taken have been directed towards the large corporates, who were responsible for 68% of outstanding non-performing loans.

Earnings Potential

Earnings for 2011 grew by 13% to USD 305 million, rebounding after steep declines of 53% and 35% the previous two years. This expansion was attributed to slight increases in net interest and commission income, and a decrease in the amount of provisions taken. Net interest income accounted for 59% of revenue generated, while commissions and profits from associates made up the majority of non-interest revenue. Going forward, we estimate net income growth in 2012 at 20%, with this expansion sustained into the future as it mirrors the increase in the bank's loans portfolio and the continued decline and normalization of provisions taken.

Growth Prospects

Total loans for 2011 were unchanged, with personal and retail loans representing the only growing segments, expanding by over 9% year-over-year. On the other hand, exposure to the government and public sector contracted by nearly 15.0% during 2011. In our forecasts, we are expecting loans to grow a CAGR of around 6.0% between 2012 and 2015, a third less than the CAGR registered over the last five years. Our loan growth forecasts resulted as a combination of estimating growth in customer deposits along with the ratio of loans-to-deposits.

We took a slightly conservative stance in forecasting customer deposits which are estimated to grow at a CAGR of around 6.3% between 2012 and 2015, in comparison to a CAGR of about 8.0% over the last five years. As for net loans-to-total deposits, we maintained the 2008-2011 average of 64.0% going forward.

Profitability Measures

Both Arab Bank's profitability measures, ROE and ROA, seem to have bottomed in 2010 and have started trending up posting slight growth in 2011. We estimate this reversal will be maintained as earnings are set to improve going forward. This recovery in profits though, hinges on the bank's ability to get NPLs under control, and provisions down to more normal levels. The company's gearing ratio (Assets/Equity) has been volatile over the last couple of years, mirroring the swings in expansion and contraction among assets held. We expect this to stabilize as the global financial crisis has calmed down, and to hover around the 6.0 level in the near future.

Valuation

We valued Arab Bank's share price at JOD 8.96 using a Dividend Discount Model (DDM) method based on 5-year forecast using a WACC of 12.7% and a terminal growth rate of 5.0%. The bank's future dividends were estimated using management's established strategy, while factoring in growth as earnings recover and expand in the coming years.

The weakness in Arab Bank's earnings as of late though has surrounded the bank's market valuation with uncertainty. When comparing Arab Bank's price-to-earnings ratio (P/E) of 20.78 to the MENA average estimated at 11.8, the Jordanian bank appears to be considerably overvalued. However, one must consider the drastic provisions that Arab Bank took over the last year, which were equivalent to 1.9% of its loans, nearly double the average provisions taken by MENA banks. When projecting a leveling out of these provisions towards the overall average, Arab Bank's adjusted P/E becomes 11.7 which is on par with the MENA average. The same analysis applies when comparing Arab Bank to the average in Jordan where the P/E for the banking sector is estimated at 13. We can therefore conclude that Arab Bank is fairly valued considering its P/E ratio.

A new development has been the recent resignation of the Chairman Abdel Hamid Shoman along with his wife and daughter, also board members. This took place after a months-long dispute with CEO Nemah Al-Sabbagh and resulted in the appointment of new chairman Sabih al-Masri. The Shoman family currently owns a 5 percent stake in Arab Bank, and the possibility of them unloading those shares will raise the near term uncertainty and selling pressure affecting the bank's stock price.

We believe Arab Bank's share price has room to appreciate and may become an attractive investment. Currently however, its share price accounts for the regional political and economic upheaval, along with the unfolding events surrounding the Chairman's resignation.

Investor Perspective

From an investor perspective, the following are certain aspects that we believe can be influencing factors and must be followed closely.

- **Regional political risk** - This is by far the most serious in our view, as an unraveling and further deterioration of the already perilous Middle Eastern situation could have a wide ranging impact and can lead to major economic and financial setbacks. Arab Bank's geographic diversification helps shield it from country specific risk, but also exposes it to the many regions undergoing economic and political transitions.
- **Credit Conditions**- Further worsening in loan repayments in some of Arab Bank's main markets would be a main point of concern. Rising NPLs among Jordanian borrowers, along with the credit worthiness of Corporate Clients in Saudi Arabia must be watched closely.
- **Provision Levels** - Arab Bank's current provision levels have been uncharacteristically high, and are unsustainable. Management's inability to normalize these levels within the coming periods would be a major red flag, and could lead to further deterioration in the company's stock price.
- **Return on Equity** - Investors have been wary of holding Arab Bank stock, as the company's Return on Equity (ROE) ratio has lagged far behind competitors. Two components have played a role in this; the decline in the bank's returns, along with the lower leverage it is operating with. ROE in 2011 was a dismal 3.9% compared to a MENA average of 12.4%. Earning recovery will be linked to improvements in credit quality as discussed already, while leverage levels will depend on management's overall strategy, which has tended in the past to remain more risk averse.

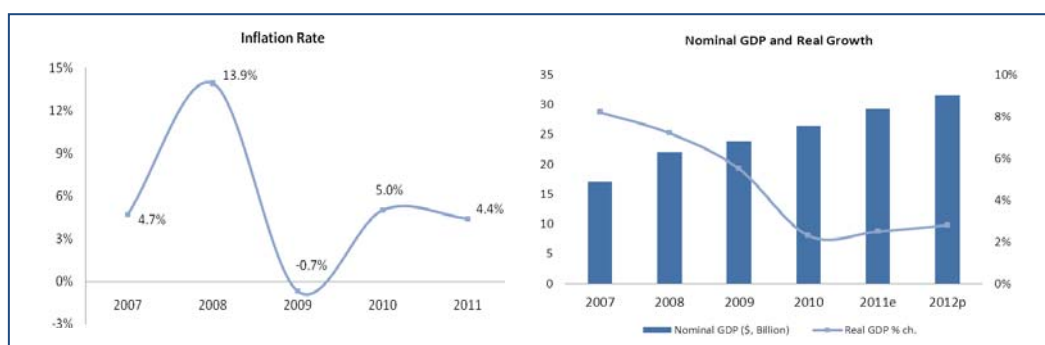
ECONOMIC OUTLOOK

Due to the regional and international diversification of Arab Bank, we touch on the economic outlook within the key markets that affect the bank's operations and profitability.

JORDAN - ECONOMY

Economic growth facing headwinds amid political instability in the region

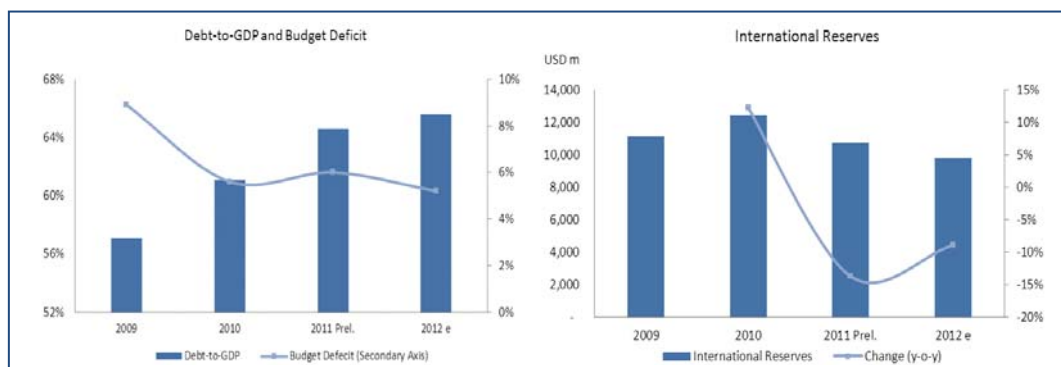
The International Monetary Fund (IMF) expected Jordan's real GDP growth to reach 2.8% in 2012 and 3% in 2013, announcing that the country's economic outlook has become increasingly challenging due to the escalating political unrest in the region and higher financing costs. Inflation stood at 3.6% in the first quarter of 2012, kept under control due to a freeze on gasoline price rises and government subsidies. Inflation averaged 4.4% in 2011 as opposed to 5% in 2010. The IMF expects the country's inflation to reach 4.9% in 2012 and 5.6% in 2013.



Source: Central Bank of Jordan, IMF

Fiscal consolidation required as IMF green-lights loan

Adverse external shocks affecting energy imports, tourism, remittances, and foreign investments have led to increased pressures with current account and budget deficits. Shortfalls in foreign direct investment along with the worsening current account conditions have led to a 14% decline in international reserves during 2011, reaching USD 10.7 billion. IMF estimates reserves to further decline to USD 9.7 billion during 2012.



Source: IMF

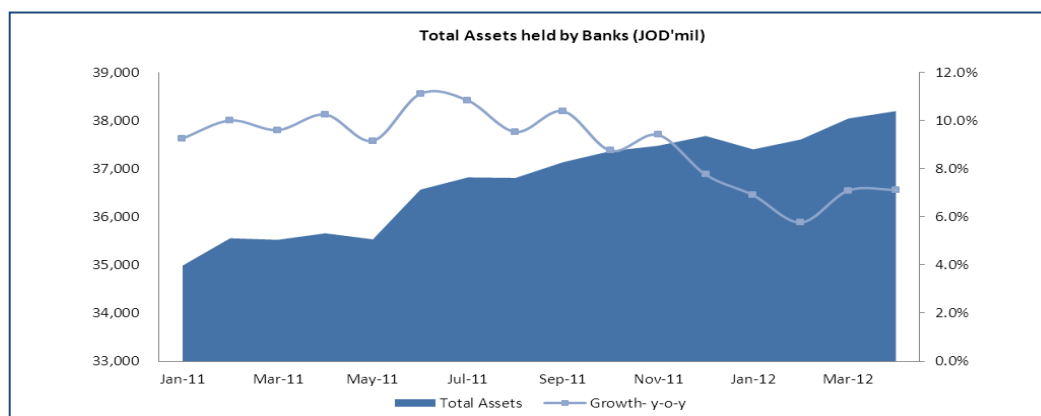
Increased social spending has aggravated the fiscal position where tighter macroeconomic policies will be needed to reduce fiscal and external imbalances. The overall fiscal deficit is expected to rise to 6% of GDP in 2011, leading to an increase in overall debt-to-GDP levels to 64.6% in 2011, from 61.1% in 2010. IMF projections for 2012 foresee a slight increase to 65.5% in debt-to-GDP levels in 2012.

Despite the rising challenges, the Jordanian authorities have proposed an ambitious fiscal consolidation plan to reduce public sector financing needs and lower public debt. This though will have to be carefully balanced against the risk of a recession and social acceptance. Confidence in this plan has been enhanced as the IMF has recently approved a USD 2 billion loan to Jordan, in the hopes that it will provide the necessary liquidity to help it get through this difficult period.

JORDAN – BANKING SECTOR

Growth in assets and deposits registered despite economic pressures

The overall volatile macroeconomic environment is expected to pressure the Jordanian banking sector going forward. Deposit and credit growth have withstood the given challenges so far, but are expected to moderate in the near term. As the government continues its implementation of austerity measures, along with the external pressures being exerted on the economy, banks are expected to maintain a conservative approach, favoring higher liquidity levels and less leverage. Having said all that, asset growth among banks seems to be stabilizing around 7% so far in 2012.

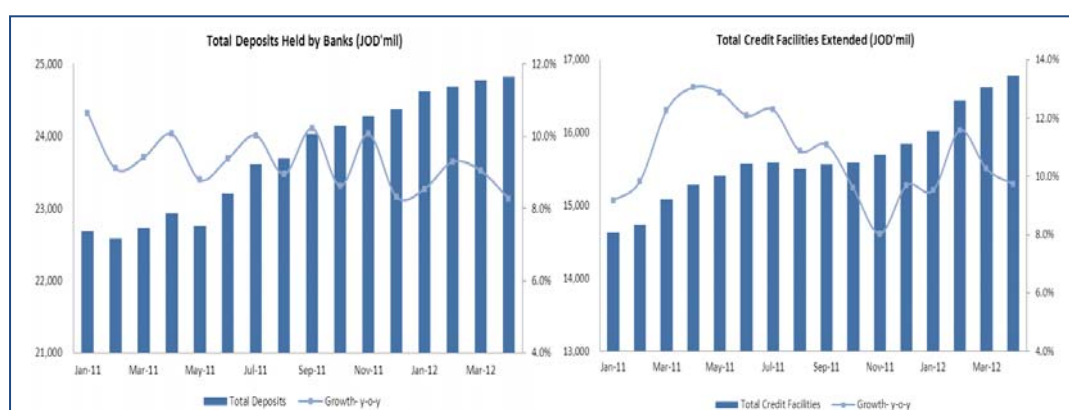


Source: Central Bank of Jordan

Deposits growth has remained relatively strong in 2012, averaging over 8% expansion year-over-year. The overall trend though seems to be declining compared to the last few years, and is expected to moderate going forward. Both internal and external economic conditions will continue to pressure deposit expansion, and must be watched closely as they form the cornerstone of the banking sector.

Rise in NPLs to force conservative approach and liquidity levels

Despite a forecasted slowdown, banking credit facilities have been resilient so far, averaging a year-over-year growth of over 10% so far. The expected economic slowdown is expected to permeate into lower loan originations, as banks will attempt to maintain higher liquidity ratios as they try to slightly minimize exposure to certain aspects within the country.



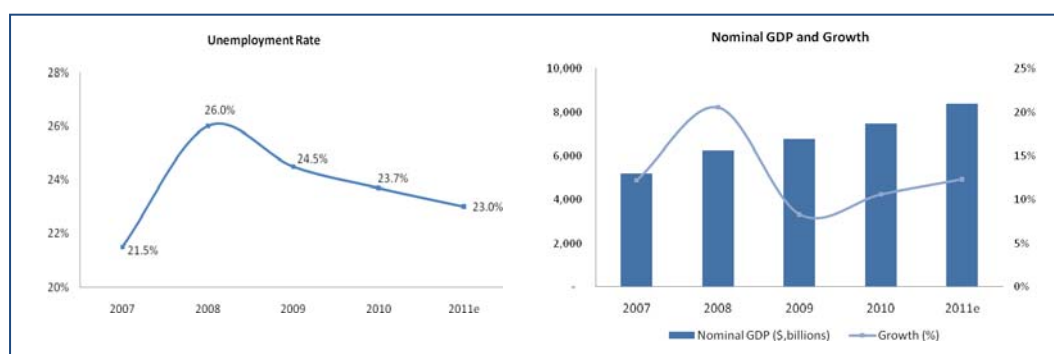
Source: Central Bank of Jordan

An ominous sign as of late has been the relatively rapid rise of bad debts, with the proportion of non-performing loans having risen in each of the past five years (reaching 8.5% in 2011, up from 4.1% in 2007). With the current instability plaguing the macroeconomic environment, this figure could trend even higher over the coming period.

PALESTINE

Positive growth trends overshadowed by high unemployment rates

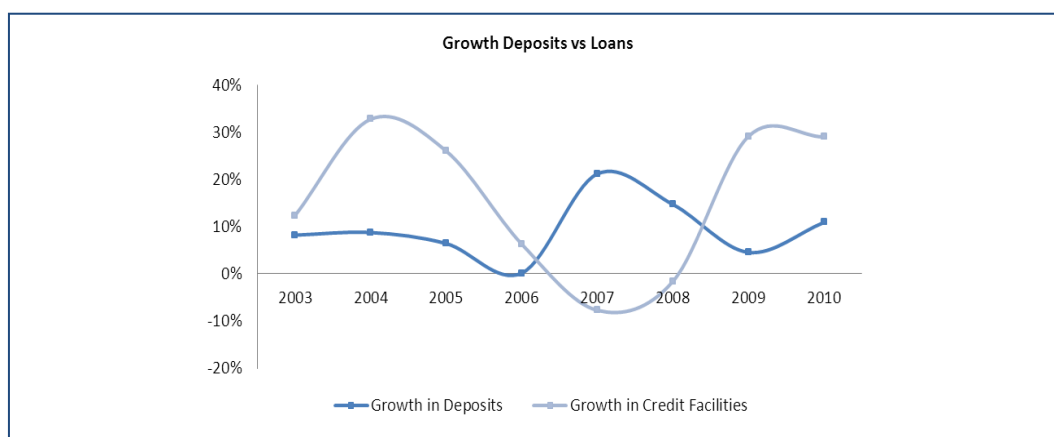
The West Bank and Gaza's economy has been growing since 2007 at over 10% per year, bolstered by aid receipts and private remittance flows. Inflation has been in the low single digits, and despite the government budget deficit remaining under control, as usual unemployment has remained excessively high at over 23%. Expectations are for current growth trends to be maintained, but with little room for a true turnaround as the Israeli government retains heavy control over the movement of people and goods.



Source: Palestinian Monetary Authority

Banking assets and deposits exhibiting solid expansion

From a banking perspective, assets held by financial institutions have averaged around 10% growth since 2006, with credit facilities expanding by 29% annually in 2009 and 2010. Growth in loans has been volatile, but overall expansion has averaged in double digits over the last 10 years. A similar story holds with resident deposits, growing by 5% and 11% during 2009 and 2010 respectively.



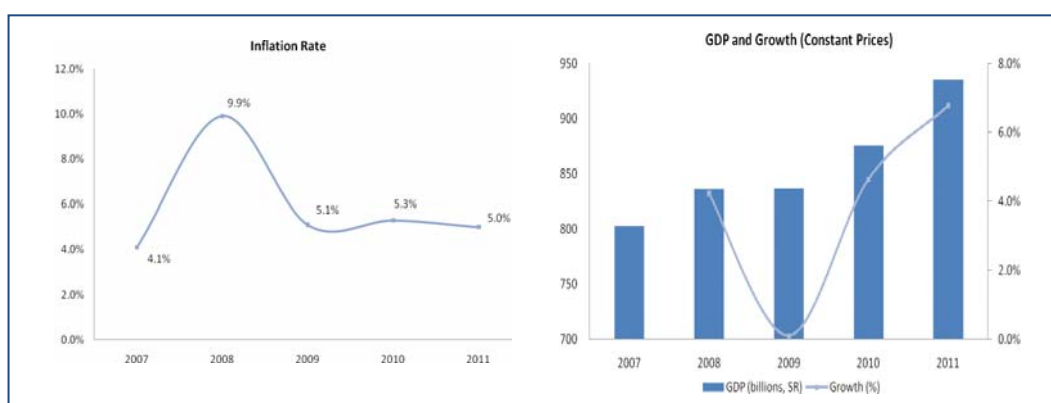
Source: Palestinian Monetary Authority

Impressive growth must be understood within the context of the prevalent situation, as conditions in the Palestinian territories remains bleak, with per capita GDP being second lowest in the Middle East only ahead of Yemen. Political risk remains the most significant deterrent, as the current regional instability, along with internal rigidity within Israel, has kept any chance of a negotiated settlement as unlikely as ever.

SAUDI ARABIA

Strong growth spurred by high oil prices and increased fiscal spending

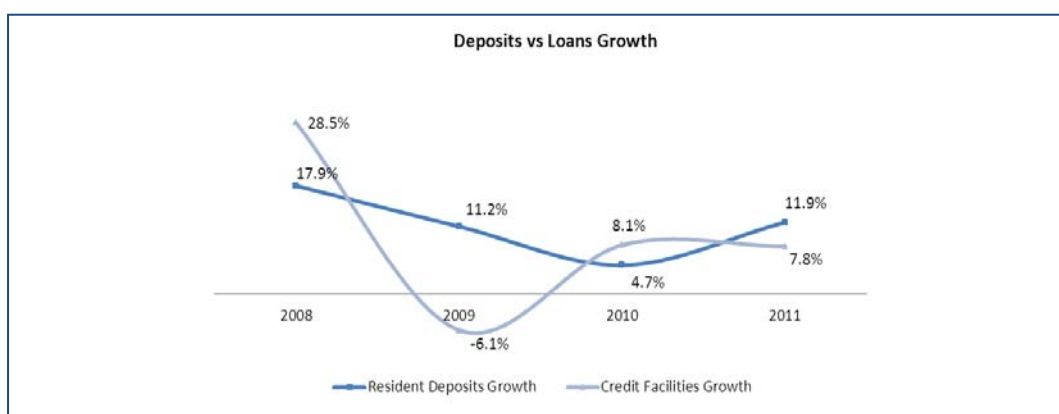
The Saudi economy continues to benefit from high oil prices and increasing global energy demand, recording impressive growth in 2011 with GDP increasing by nearly 7.0%. Expansion was bolstered by increased crude production, along with the implementation of large scale fiscal stimulus plans. Expectations are for expansion to be maintained at a slightly slower pace, as lower oil production (as they make way for returning Libyan output) and lower government spending take effect. High oil prices should help further confidence within the economy, as internal consumption growth is expected to remain strong. Inflation seems to be stabilizing around 5%, with unemployment still relatively high at over 10%.



Source: Palestinian Monetary Authority

Expansion within banking sector mirrors strong growth in economy

Banking assets were spurred by the boost in the economy, growing by 9% in 2011. This expansion was mirrored by similar growth among resident deposits and credit facilities, increasing by 11.8% and 7.8% respectively. The outlook is for the positive trend to be maintained as internal demand continues to be strong.



Source: Palestinian Monetary Authority

Despite the many headwinds experienced over the past few years, the Saudi banking sector seems to have overcome the period with little shocks to the system. The full backing of the government, along with a more conservative approach has allowed these banks to avoid some of the asset deterioration experienced among others in the GCC. The only real worry for Saudi banks has been in the corporate sector, as troubles and restructurings among some large corporations could leave banks slightly vulnerable.

NORTH AFRICA

Potential repressed by unfolding political changes

The theme within North Africa is of great potential which is marred by ongoing political instability. Revolutions and uprisings have left governments in a rather weakened state, failing to instill confidence in investors for long term commitments. High youthful unemployment lingers as a core threat, with some countries like Egypt also dealing with high inflation. GDP growth remains in the low single digits with uncertainty clouding outlook in the near term. Among the countries there, Algeria stands out due to the abundance of natural resources, along with Morocco as the political situation has been relatively more stable. Overall presence in North Africa remains a viable long term strategy which can be beneficial as these young economies transit into more mature and stable ones.

EUROPE

Austerity measures set to push economies back into recession

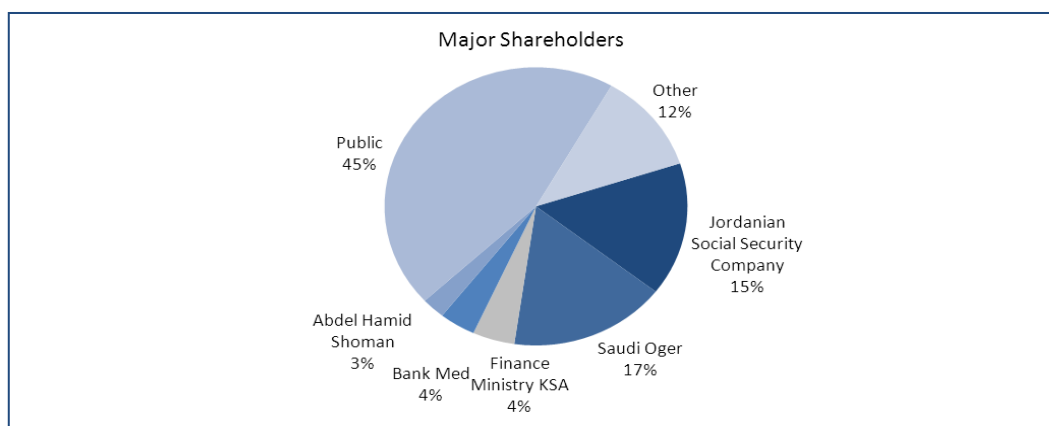
The economic problems plaguing the European continent have been widely publicized, with over indebtedness being at the core of most of these issues. From over leveraged banks to highly indebted sovereigns, the economic outlook within Europe remains bleak with harsh austerity measures looming as the only viable solution barring defaults and restructuring. Political instability is expected to rise if conditions deteriorate, with most economies sliding back into recession. Presence in Europe though remains vital, as solid and safe institutions are set to benefit from the unfolding flight to quality environment.

COMPANY PROFILE

Arab Bank was established in Jerusalem, Palestine in 1930 and has since grown into one of the largest financial institutions in the Middle East. Headquartered in Amman, Jordan, it currently boasts over 500 branches in 30 countries, participating in financial markets and centers worldwide. It is engaged in the offering of products and services such as consumer banking, corporate and investment banking, and treasury. Arab Bank caters to serve the needs of individuals, corporations, government agencies and other international financial institutions. Currently, it has over USD 31 billion of customer deposits, which have grown by over USD 7 billion since the global financial crisis in 2008. In Jordan, it is the largest financial institution in terms of assets, equity, capital, and banking market share

Ownership

Arab Bank was the first public shareholding company listed on the Amman Stock Exchange in 1978, and currently has the largest market capitalization, representing 28% of the exchange. It has 534 million shares outstanding, with a 46% float ratio. The shareholding structure is very stable and diverse, with the four largest shareholders being committed long term investors in the bank. These four are: the Harriri Family - 21.74% (through Saudi Oger, Bank Med and Bank Med Suisse), the Jordanian Social Security Corporation - 15.50%, the Saudi Finance Ministry - 4.50%, and the founding Shoman family - 4.03%.



Source: Arab Bank

Management

Name	Position
Mr. Nemeh Elias Sabbagh	Chief Executive Officer
Ms. Randa Muhammad Sadik	Deputy Chief Executive Officer
Dr. "Mohammad Ghaith" Ali Mohammad Mismar	General Counsel
Mr. Ghassan Hanna Suleiman Tarazi	Chief Financial Officer
Mr. Mohamed A. Hamad Ghanameh	Head of Credit
Mr. Samer S. Tamimi	Head of Corp.and Investment Banking
Mr. Antonio Mancuso-Marcello	Head of Treasury
Mr. Naim Rassem Kamel Al-Hussaini	Head of Consumer Banking
Mr. George Fouad El-Hage	Chief Risk Officer

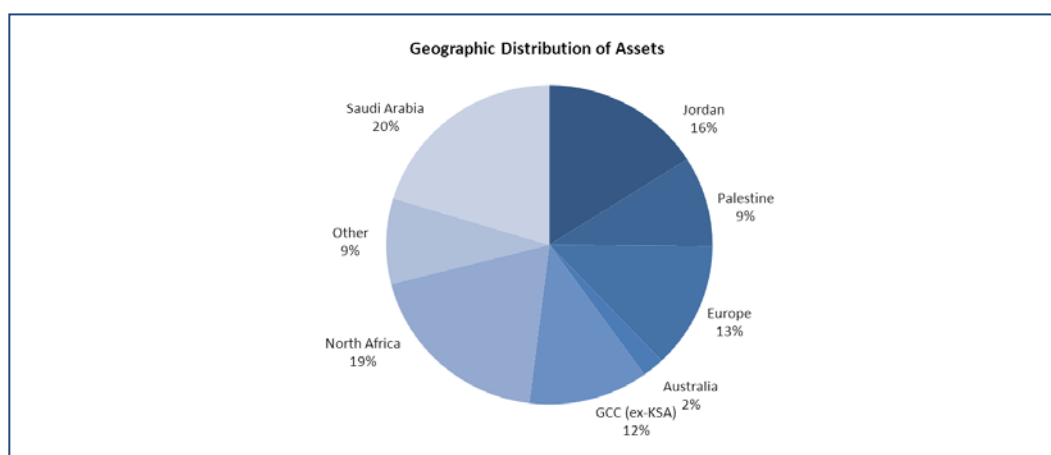
Source: Arab Bank

Arab Bank Group Structure

Arab Bank Group's structure is made up of 3 parts:

1. **Arab Bank Plc** - This incorporates the main bank and its operations, which are headquartered in Amman, Jordan, and have a presence throughout the Middle East and North Africa.
2. **Subsidiaries** - These are described below, and are companies in which Arab Bank controls over 50% of outstanding shares.
3. **Associates** - These are affiliate companies in which Arab Bank has less than a 50% stake.

The bank has utilized an aggressive expansionary strategy over the years to gain exposure to markets around the globe. Including share of assets controlled in associates, the geographic distribution of assets is as follows.



Source: Arab Bank

Once considering all assets under management, a highly diversified and balanced mix is revealed. Presence in Saudi Arabia, through Arab National Bank of which Arab Bank owns 40%, is the largest one country exposure the bank carries. This is followed by 16% of the bank's assets being in Jordan, and 9% in Palestine.

Arab Bank also has excellent exposure to Western developed nations, with 13% of overall assets found on the European continent, and another 2% in Australia.

Earnings Exposure

As is expected with the global diversification of assets, the sources of Arab Bank's revenue streams are just as varied. The bank's earnings are generated through branches directly operated by Arab Bank Plc., and through the subsidiaries and associates owned around the world.

In 2011, Arab Bank Plc. earned a net income of USD 370 million. 27% of the revenue was obtained inside Jordan, while the rest was through its other branches with a heavy presence in the Palestinian territories.

Activities in Europe, which represent the largest component of assets among subsidiaries, struggled this year, posting a loss of nearly USD 54 million. As for associates, Arab Bank's share of profits for 2011 was equivalent to over USD 265 million. Almost 87% of this was earned through Arab National Bank in Saudi Arabia, while 11% came from Oman Arab Bank.

Subsidiaries

Arab Bank has a global presence with investments in subsidiaries around the world.

Subsidiary	Ownership %	Location	Activity	Paid-up Capital
Europe Arab Bank plc	100	U.K	Banking	USD 687m
Arab Bank Australia Limited	100	Australia	Banking	USD 62m
Islamic International Arab Bank	100	Jordan	Banking	USD 140m
Arab National Leasing Company Ltd	100	Jordan	Finance/ leasing	USD 21m
Al-Arabi Investment Group Ltd	100	Jordan	Finance/ leasing	USD 19m
Arab Sudanese Bank Limited	100	Sudan	Banking	USD 43m
Arab Investment Bank S.A.L	66	Lebanon	Banking	USD 10m
Arab Tunisian Bank	64	Tunisia	Banking	USD 62m
Al Arabi Capital Limited	-	U.A.E	Finance/ leasing	-
Al Arabi Inv.Group Limited - Palestine	100	Palestine	Finance/ leasing	USD 14m
Al-Nisr Al Arabi plc	50	Jordan	Insurance	USD 2.3m
Arab Bank Syria	51	Syria	Banking	USD 78m

Source: Arab Bank

Major Subsidiaries

Europe Arab Bank plc

Europe Arab Bank plc (EAB) is a limited liability company established in 2006 with paid-up capital of USD 687 Million. The Bank is a wholly owned subsidiary of Arab Bank plc, with its headquarters in London. EAB has a European passport that enables it to open branches anywhere in the European Union. Through a network of seven branches operating in UK, Austria, France, Germany, Italy and Spain, EAB provides all types of banking products and services, including private banking and treasury services, to its customers.

Arab Bank Australia Limited

Arab Bank Australia Limited was founded in Australia in 1994 with paid-up capital of USD 62 million. The bank is a wholly owned subsidiary of Arab Bank plc. Through a network of 10 branches, this subsidiary provides all commercial and retail banking products and services to its Australian customers.

Islamic International Arab Bank plc

It's a wholly owned subsidiary of Arab Bank that was founded in Jordan in 1997 with paid-up capital of USD 140 million. It offers a full range of banking products and services, which are in accordance with Islamic Sharia rules through a network of 32 branches spread across Jordan.

Sister Company

Arab Bank (Switzerland) Limited

Founded in 1962 in accordance with Swiss law, Arab Bank (Switzerland) is an independent bank that is owned by the very same shareholders of Arab Bank plc. It has two main areas of activity through a network of two branches: private banking, which covers asset and investment management for both private and institutional clients in addition to trade financing. As of the end of 2011, total shareholders' equity was equal to CHF 493 million, with total assets at CHF 2.45 billion.

Affiliates

Arab Bank's investments in Affiliated Companies as of 31/12/2011:

Name of Company	Principal Activity	Ownership %	Cost (USD'000)	Country
Turkland Bank	Banking	50%	172,268	Turkey
Oman Arab Bank	Banking	49%	204,903	Oman
Arab National Bank	Banking	40%	1,817,000	Saudi Arabia
Arabian Insurance Co.	Insurance	36.79%	37,423	Lebanon
Commercial Building Co.	Real Estate	35.24%	13,169	Lebanon

Source: Arab Bank

Major Affiliate

Arab National Bank

The Arab National Bank (ANB) is a major bank based in Riyadh, Saudi Arabia and listed on the Saudi Stock Exchange. It is among the top ten largest banks in the Middle East and has received an 'A' rating from Standard and Poor's. It caters for the diverse needs of its Corporate and Retail clients. To service a large and varied customer base which exceeds 2 million, the Bank has an extensive distribution network, with over 270 premises spanning the Kingdom. These include over 185 branches (of which 25% are Ladies' Branches) and 85 remittance centers (TeleMoney). ANB is the 2nd largest provider of remittance services in the Kingdom.

In 2011, ANB's net income was equal to USD 579 million. Total Assets were equivalent to USD 33.4 billion, and Customer Deposits to USD 24.2 billion.

Arab Bank Credit Rating

Fitch has recently affirmed Arab Bank Plc.'s Long term Issuer Default Rating (IDR) at 'A-' with a Stable Outlook. The Viability Rating (VR) has also been affirmed at 'a-'.

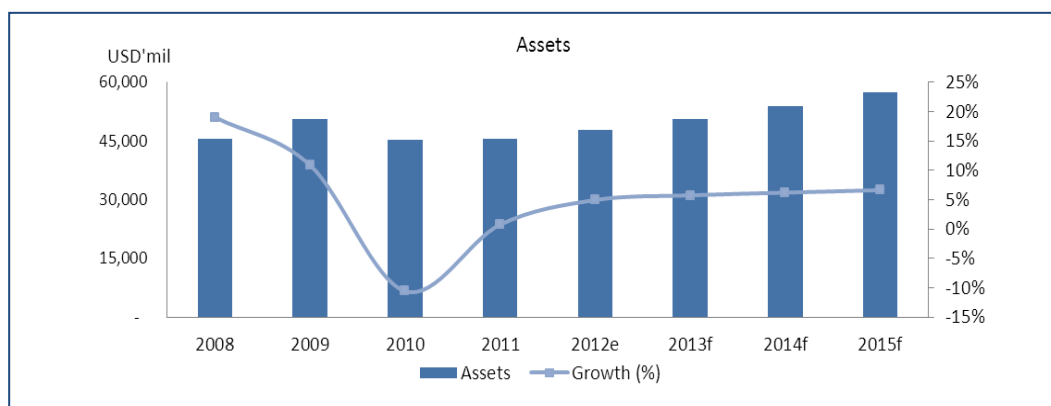
When rating Arab Bank, the analysis and the rating drivers take into account the balance sheet strength and performance of the group as a whole. Although domiciled in Jordan, Arab Bank's ratings are not considered to be constrained by Fitch's view of the Jordanian sovereign because of the group's geographic diversification of assets as shown above.

The stable outlook reflects the bank's overall sound risk profile, solid capital and strong liquidity. Nonetheless, it also considers the increasing risks (mostly credit) associated with the bank's operations across the MENA region, specifically in the 'Arab Spring' countries. The risks are increasing as a result of the unrest and economic slowdown. Although the effects have so far been manageable for Arab Bank, there is increasing negative pressure on the ratings.

ASSETS

Assets steady at over USD 45 billion

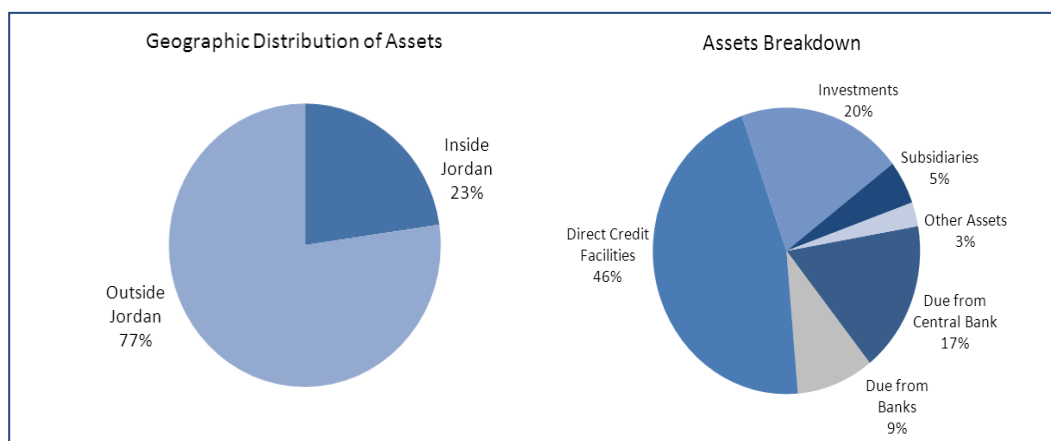
As of the end of 2011, Arab Bank's assets stood at over USD 45 billion, expanding by 1% after an 11% decline a year earlier. Assets had shown strong and steady increases as Arab Bank's perceived reputation as a safe haven bank helped it post double digit growth during the global economic downturn of 2008/2009. However, assets reverted back to previous levels as the financial markets stabilized. Looking forward, we took a conservative approach forecasting moderate growth in assets of 5-7% through 2015.



Source: Arab Bank

Geographic diversity shields against country specific risk

With presence in over 30 countries, assets are diversified geographically with only a 23% concentration in the bank's main market of Jordan. This helps shield the bank from risks arising within a specific market, but has also exposed the bank to some of the turmoil arising in the Arab world. Even though this has not affected growth so far, decisions like deconsolidating its Libyan subsidiary, Wahda Bank, were taken as management continues its risk-averse approach.



Source: Arab Bank

Asset Breakdown and Liquidity

Direct Credit Facilities represented the largest component of assets held by Arab Bank, making up 46%, or around USD 21 billion. These are broken down in detail in the loan portfolio section below. The next largest asset class is the investments and financial securities held by the bank. These represented nearly 20% (USD 9.1billion) of overall bank assets, and have been concentrated in highly liquid, highly rated securities. Only about 9% of these investments are in stocks and mutual funds (1.8% of Assets), with around 85% invested in Government and Corporate bonds (at least A- rated).

Investments	
AAA to A-/Investments	18.7%
Government and Public Sector/Investments	65.9%
Below A-	6.29%
Stocks and Mutual Funds	9.02%
Highly Rated	84.6%

Source: Arab Bank

As the economic and political environments have become increasingly volatile, ARBK management have made a significant effort to maintain high liquidity at all times. In 2011, the bank's cash and cash equivalents made up 46% of the balance sheet, and ranged between 42% and 50% over the last five years.

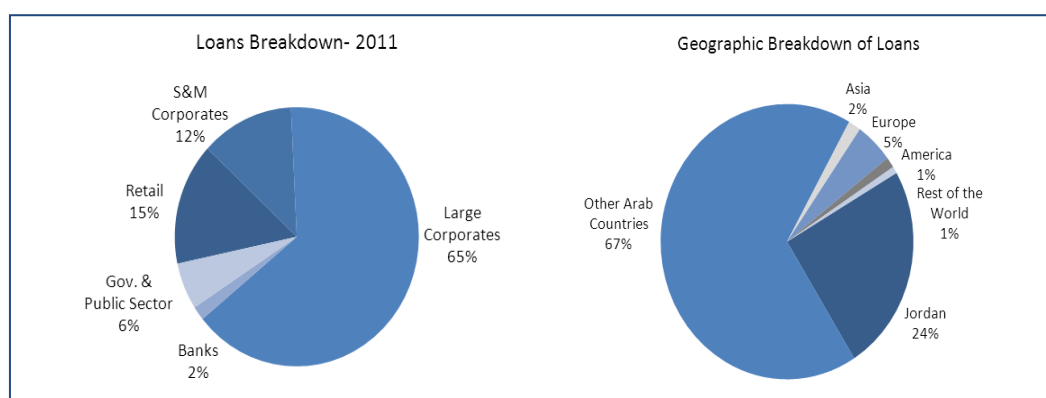
(000'USD)	2007	2008	2009	2010	2011
Cash and Due from Banks	9,452,433	12,712,293	16,241,589	12,445,254	12,048,353
Investment Portfolio	6,799,133	7,005,710	8,787,624	7,914,782	9,129,494
Total Assets	38,333,304	45,629,599	50,600,589	45,262,533	45,613,211
Liquidity Ratio	42.4%	43.2%	49.5%	45.0%	46.4%

Source: Arab Bank

LOANS

Impressive loan diversification among customer base, geographic region, and economic sectors

ARBK's direct credit facilities reveal a highly diversified loan portfolio with exposure to an array of sectors and geographic regions. These loans have been focused towards a mix of borrowers, with the main emphasis being on Corporates. In 2011, Large Corporates accounted for 65% of the loans portfolio, with Small and Medium Corporates making up another 12%. This emphasis has been in line with the bank's overall strategy of maintaining higher exposure to well established large institutions. Credit directed towards retail consumers only accounted for 15%, but also witnessed the largest growth year over year at 9%, resembling a promising area where future expansion can take place.



Source: Arab Bank

Geographical diversity among the loans issued is another important aspect of the management's strategy, with Jordan receiving only 24% of credit lent. Other Arab countries, where the majority of Arab Bank branches are located, accounted for 52% of the loans originated. This diverse approach is critical in creating both a growing presence in new markets, as well as in minimizing the risk arising from concentrating on one region.

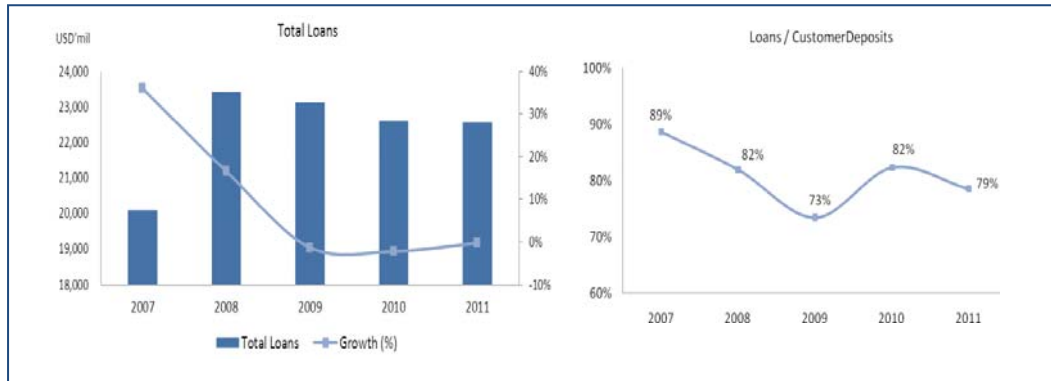
A closer look at corporate loans, which constitute nearly 77% of the portfolio, reveals that exposure is diversified among all economic sectors. The Industry & Mining sector had the largest share at 20.7%, with a prominent presence within both the Trade and General Services sectors, accounting for 16.0% and 12.9% respectively.

Corporate Loans							
Industry & Mining	Construction	Real Estate	Trade	Agriculture	Tourism & Hotels	Transportations	General Services
20.7%	7.55%	8.81%	16.0%	0.83%	3.88%	6.36%	12.9%

Source: Arab Bank

Loans vs. Deposits

Declining interest rates and the volatile economic conditions have led to a slowdown in the growth of loans, with overall credit slightly contracting over the last three years. In 2011, ARBK's loans outstanding remained unchanged year over year, an important sign that bank lending is stabilizing. The ratio of loans-to-customer deposits has been declining during the past few years due to Arab Bank's careful approach in issuing loans, thus leading to a ratio of 79% for 2011 compared to 89% in 2007.



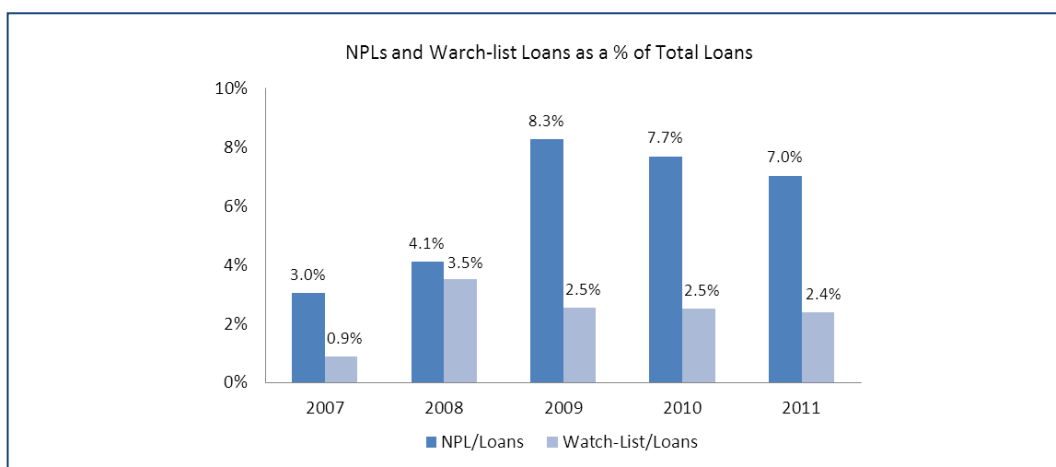
Source: Arab Bank

Going forward, we forecast management maintaining a reserved credit policy with a stable loans-to-customer deposits ratio of around 78%.

CREDIT QUALITY

Credit quality improvements signal reversal to previous deterioration

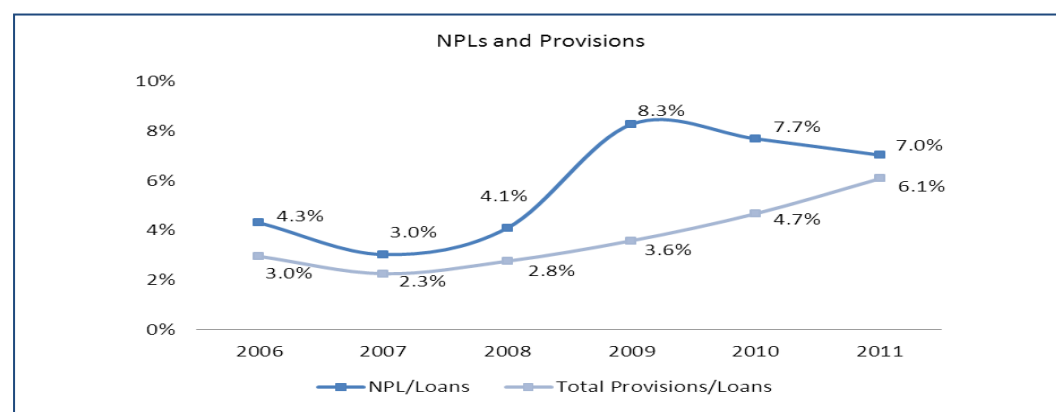
Arab Bank's credit quality saw slight improvements in 2011, signaling a reversal in the worsening conditions of the previous two years. Watch-list loans (which are loans that may become non-performing) remained stable as a percentage of total loans around 2.5%, with non-performing loans improving from a high of 8.3% in 2009 down to 7% in 2011. In absolute terms, non-performing loans have been steadily declining at around 9% per year since peaking in 2009. The majority of those loans along with the provisions taken have been directed towards the large Corporates, who account for 68% of the non-performing loans outstanding.



Source: Arab Bank

Provision levels remain too elevated

Accompanying the rise in non-performing loans, total provisions have skyrocketed from around USD 450 million in 2007, to nearly USD 1.4 billion as of the end of 2011. This represented an increase in total provisions to loans from around 2.3% in 2007 vs. around 6.1% in 2011. Increased provisions have had a sizeable effect on the company's earnings, and should be watched carefully as a return to more normal levels will translate into an improved bottom line.



Source: Arab Bank

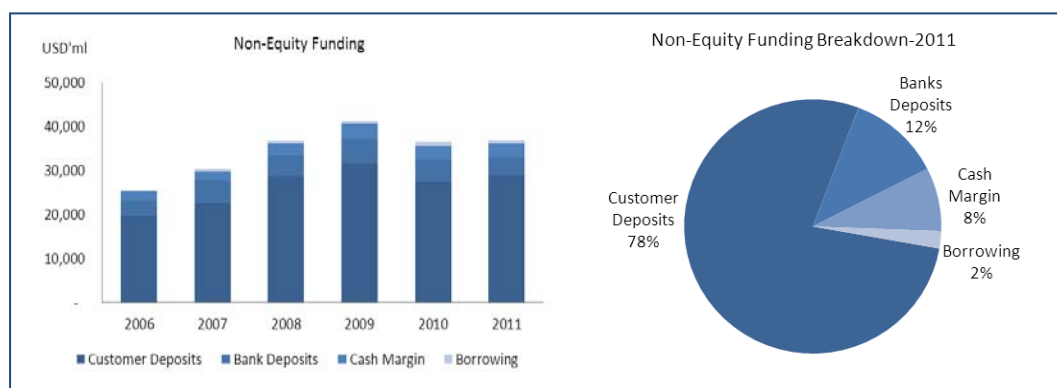
(%)	2006	2007	2008	2009	2010	2011
NPL Coverage Ratio	68.6	74.5	67.4	43.3	60.8	86.5
NPL/Loans	4.3	3.0	4.1	8.3	7.7	7.0
Watch-List/Loans	0.9	0.9	3.5	2.5	2.5	2.4
Provisions/Loans	0.17	0.13	0.17	0.88	2.09	1.93

Source: Arab Bank

NON-EQUITY FUNDING

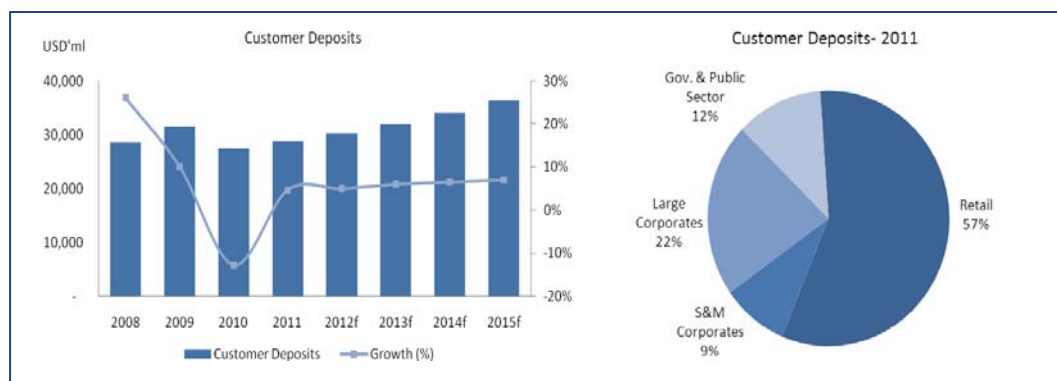
Main funding through customer deposits with little reliance on debt

Arab Bank's non-equity funding relies very little on debt, of which only 10% is from long term borrowing and cash margin. Banks & Financial Institution deposits account for 12%, leaving customer deposits as the main source of funding at 78% as of end 2011.



Source: Arab Bank

As with assets, customer deposits in 2011 saw a return to growth estimated at 5% after a steep decline of 13% a year earlier. Despite the recent volatility, they are reported to have grown by over a billion dollars since 2010, and over 6 billion dollars since 2007. We estimated the CAGR over the past 5 years to be around 8% and expect this positive trend to continue but at a slightly lower rate.



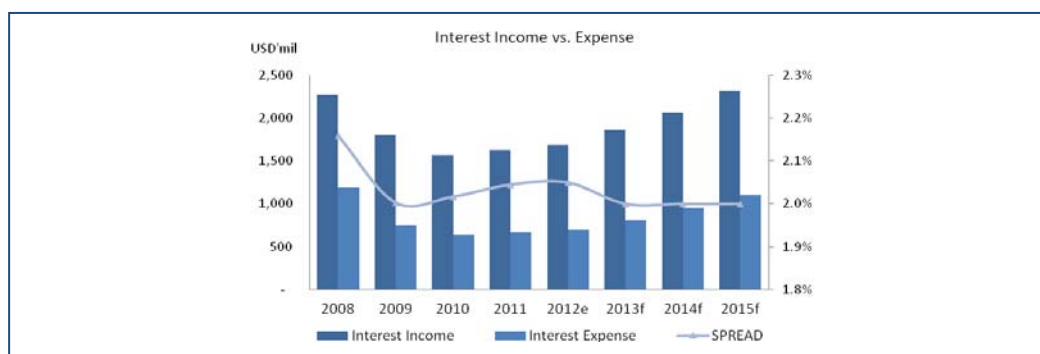
Source: Arab Bank

Arab Bank also boasts a diverse base of customer deposits, with only 57% coming from retail customers, 31% from corporations and 12% from government and public entities.

INCOME BREAKDOWN

Expansion in interest income as interest spread remains stable

In 2011, Arab Bank's gross interest income grew by over 3.5% to USD 1.62 billion. The increase came despite the bank's loan book remaining unchanged, as rates on credit handed out have moved upwards. Interest expense also grew by around 5%, reflecting the addition in customer deposits held. The spread between interest income and expenses has remained very stable around 2.0%, and we expect this to be maintained going forward.



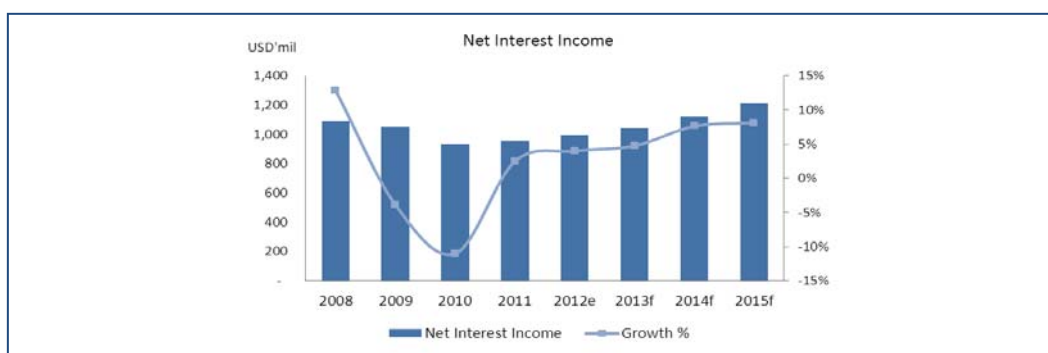
Source: Arab Bank

Global drop in interest rates hurts earnings

Despite sustaining a consistent spread, the overall decline in interest rates since 2008 has had a negative effect on income as expected. Returns on loans averaged 5.28% in 2011, versus 6.27% in 2008. Likewise, payments on customer deposits averaged 1.78% in 2011, versus 2.75% in 2008. Since Arab Bank uses very little debt, they have been unable to take advantage of the declining cost of capital.

Average Returns on Assets	2008	2009	2010	2011
Loans	6.27%	5.34%	4.92%	5.28%
Funds w/ Central Bank	2.72%	1.23%	1.06%	1.03%
Funds w/ Banks and Institutions	4.40%	1.38%	1.00%	0.49%
Investments (Bonds & Stocks)	6.24%	4.70%	4.90%	4.56%
Weighted Return on Assets	5.39%	3.82%	3.76%	3.85%

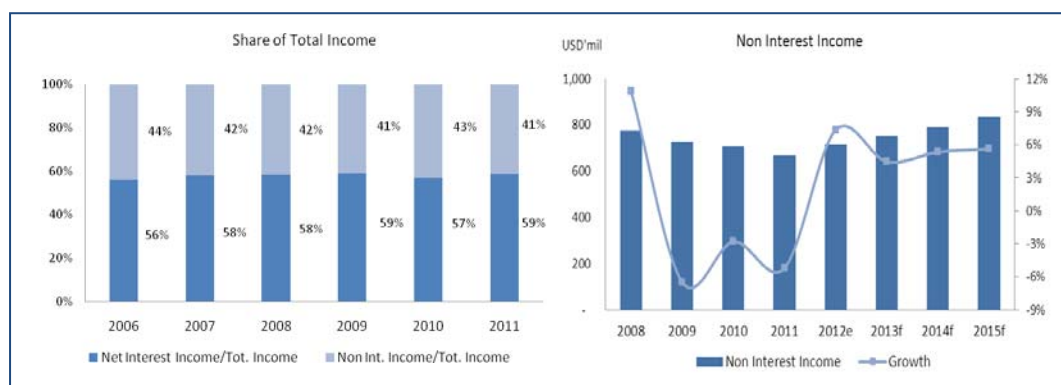
Average Costs of Liabilities	2008	2009	2010	2011
Customer deposits	2.75%	1.82%	1.76%	1.78%
Banks and Institution deposits	4.52%	1.55%	1.69%	1.61%
Cash Margin	5.37%	1.87%	1.44%	1.67%
Borrowed funds	4.51%	1.44%	0.98%	2.51%
Weighted Cost of Liabilities	3.23%	1.81%	1.74%	1.81%



Source: Arab Bank

Interest income captures higher share of revenues

Net interest income, which grew by 2.5% in 2011, accounted for around 59% of income generated (including profits from associates). This level has fluctuated from around 56% up to near 60% over the last several years. As for non-interest income (which is comprised of net commissions, profits from associates, and other revenue), it made up the remaining 41% of returns after declining by 5.2% in 2011. This was mostly due to a 41% contraction in Other Revenue, as Net Commission income grew by 2.5%, and profits from associates increased by 7.2%.



Source: Arab Bank

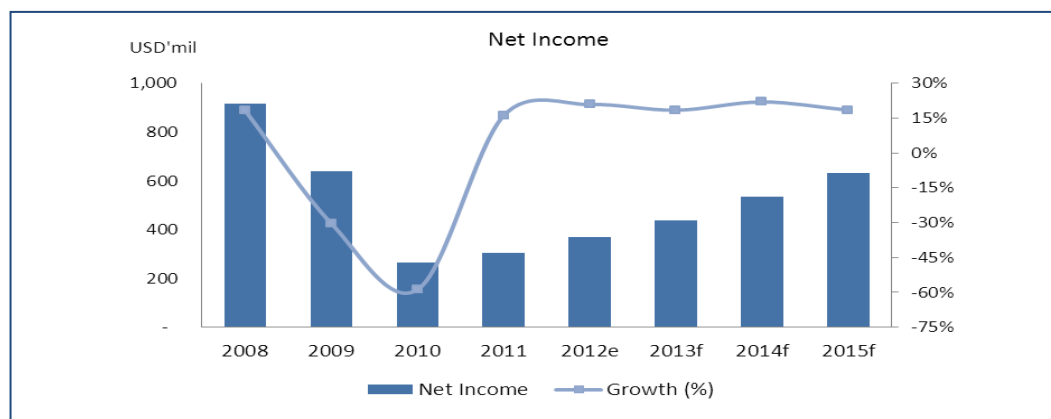
Revenue Breakdown	
Total Revenue Breakdown	
Interest Income	59.40%
Non-Interest Income	40.60%
	100.00%
Interest Income Breakdown	
Direct Credit Facilities	68.10%
Financial Assets & Investments	25.60%
Deposits w/ Central Bank & other FI	6.20%
	100.00%
Direct Credit Facilities Breakdown	
Loans and advances	64.23%
Overdrafts	21.10%
Real – estate loans	9.14%
Discounted bills	4.20%
Credit cards	1.33%
	100.00%
Loans and Advances Breakdown	
Large Corporates	56.37%
Retail	20.92%
S&M Corporates	16.00%
Gov. & Pub. Sector	5.38%
Banks & FI	1.33%
	100.00%

Source: Arab Bank

PROFITABILITY

Double digit growth in earnings puts end to 2 year decline

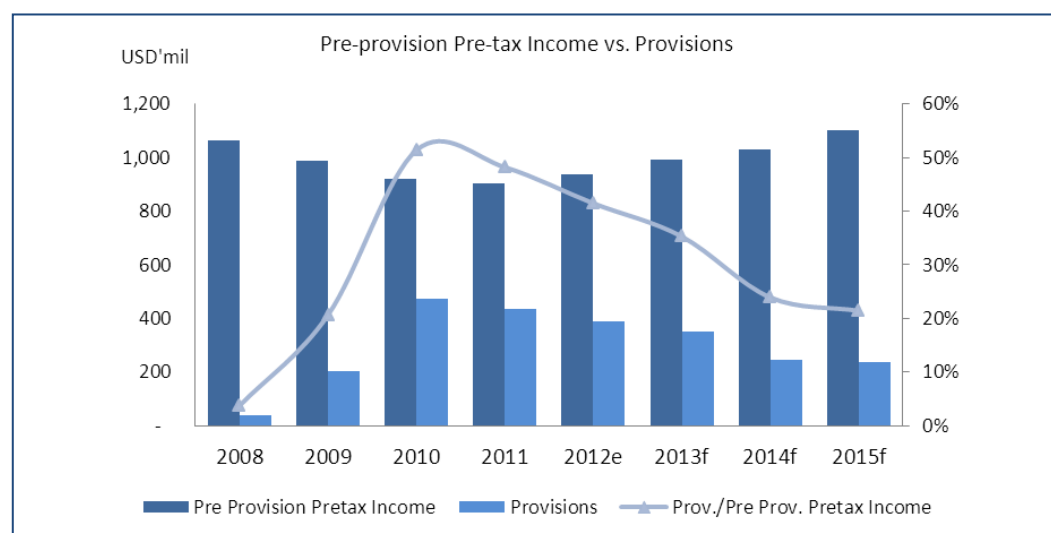
Earnings for the year grew by 13% to USD 305 million, putting an end to the steep declines of the previous two years. This expansion was attributed to slight increases in interest and commission income, and a decrease in provisions taken. Going forward, we forecast continued growth in net income, mirroring the expansion of the bank's loan portfolio and the continued decline and normalization of provisions taken.



Source: Arab Bank

Provision levels high vs. pre-tax income

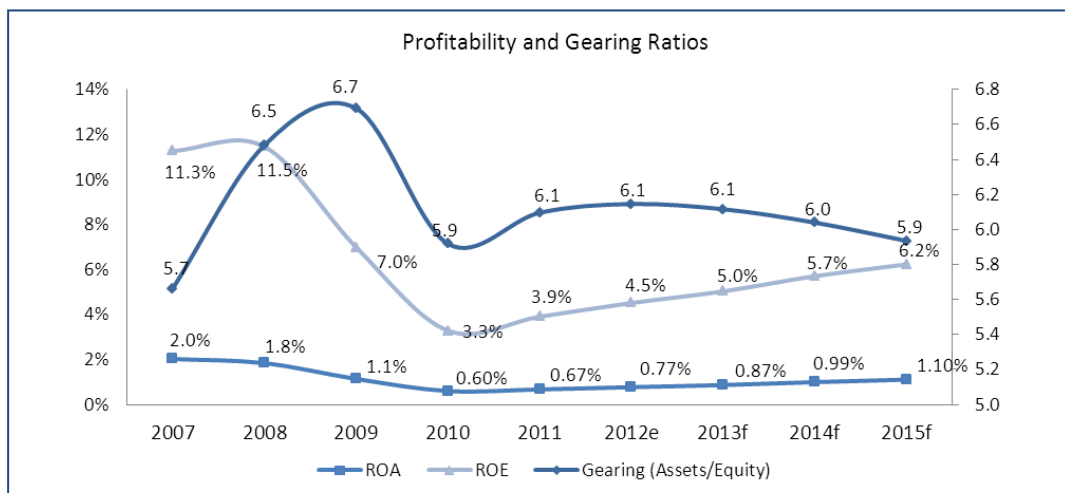
As non-performing loans spiked up over the last several years, the provisions taken have had a serious impact on the bottom line. Provisions set aside in 2007 totaled USD 450 million, while in 2011 they ballooned to nearly USD 1.4 billion. Leading up to 2009, provisions recognized had been stable, making up around 4% of pre-tax income. Since then that amount has drastically increased to make up around 50% of pre-tax income during 2010 and 2011. This has had devastating effects on overall earnings, and as these levels normalize going forward we expect profitability to greatly improve.



Source: Arab Bank

Profitability ratios trending up after bottoming out in 2010

Both ARBK's profitability ratios, ROE and ROA, seem to have bottomed in 2010, and have started trending up posting slight growth in 2011. We estimate this reversal will be maintained as earnings are set to improve going forward. The company's gearing ratio has been volatile over the last couple of years, mirroring the swings in expansion and contraction among assets held. We expect this to stabilize as the global financial crisis has calmed down, and to hover around the 6.0 level in the near future.



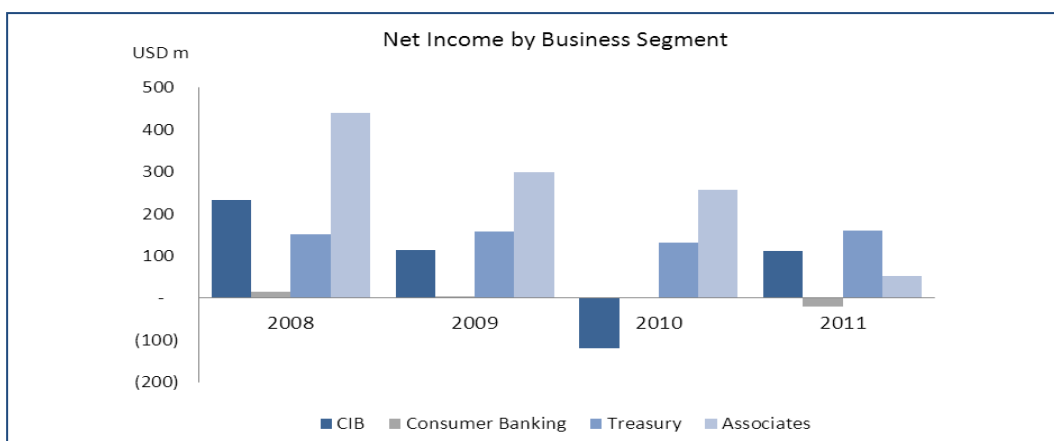
Source: Arab Bank

Business Segments

The turmoil plaguing the financial markets has affected performance within all business segments. Two main factors influencing the bottom line have been the diminishing interest rates, along with the rising provisions.

Corporate and Investment Banking (CIB): Turnaround on lower provisions

The Corporate and Investment Banking (CIB) division witnessed a return to profitability in 2011, netting USD112 million in income. This business segment has been plagued by the majority of provisions incurred, and the 2011 performance is a positive indicator of a possible reversal in trend.



Source: Arab Bank

Consumer Banking: Disappointing performance

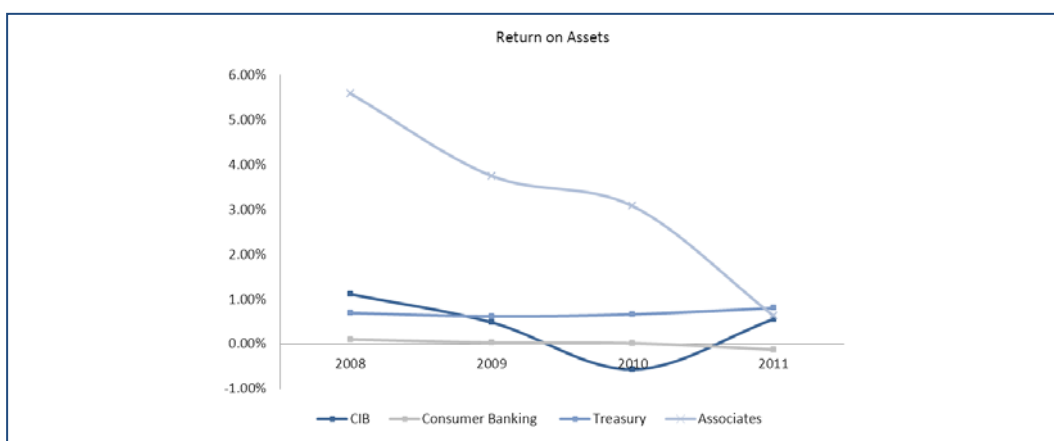
Since 2008, consumer banking has performed the worst among Arab Bank's business segments, providing negligible returns year after year. In 2011, net income within the consumer banking division was equal to a loss of USD 21 million, the only money losing segment within the bank.

Treasury Operations: Consistent

Treasury operations have been the most consistent, posting USD161 million in returns in 2011. It has also been the only segment to record an expansion in profits compared to 2008. Return on assets within this division was 0.80%, the highest returns among all segments in 2011.

Associates: Steep Decline

Profit from associates has had a significantly positive impact on the bank's returns since 2008, shielding it from the diminishing returns within its other divisions. This however took a sharp downturn in 2011, with net income from associates declining to USD53 million from USD256 million in 2010, due to a rise in provisions within its operations.

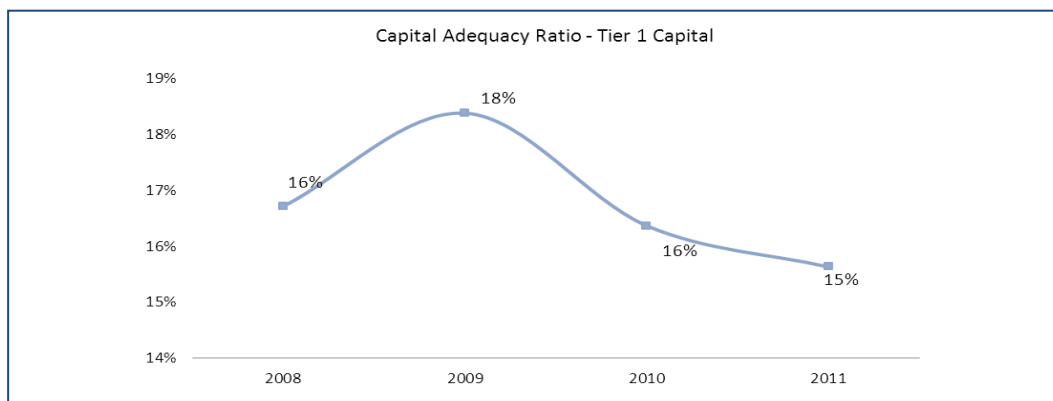


Source: Arab Bank

EQUITY

Capital base solid with Tier-1 ratio significantly higher than required

The bank's capital base contracted by around 2% in 2011, declining to about USD 7.7 billion as of the end of the year. In line with management's overall conservative approach, the capital adequacy ratio stood at 15.1%, which far exceeds the 8% minimum required by the Basel II Committee, and the 12% minimum required by the Jordanian Central Bank. Arab bank's solid capital base can withstand further credit deterioration even though this is unlikely, and gives management a chance to increase the bank's leverage if they wish to do so.



Source: Arab Bank

Dividend Payout Policy

With regards to the cash dividends, Arab Bank follows an established policy of distributing between 20-30% of its share's par value. In 2011, the Board of Directors recommended the distribution of cash dividends of 25%, or JOD 133.5million, compared to 20%, or JOD 106million for the year 2010.

	2007	2008	2009	2010	2011
EPS (USD)	1.43	1.51	0.99	0.47	0.55
BVPS (USD)	12.7	13.2	14.2	14.3	14.0
Div. as % of Share Par Value	30%	25%	20%	20%	25%
Dividend Yield (end of year)	1.02%	1.64%	1.65%	2.00%	3.18%

Source: Arab Bank, BlomInvest

COMPARABLE ANALYSIS

In order to assess the performance of Arab Bank in comparison to other banks in the region, we compare it on three different fronts:

1. Relative Valuation: Shows how the market perceives the bank (overvalued, undervalued, or fairly valued).
2. Capital Structure and Policy: Shows how conservative the company is in issuing loans with respect to its deposits as well as taking provisions in comparison to others.
3. Profitability: Shows management's effectiveness in generating income using its assets and transmitting it through to equity holders.

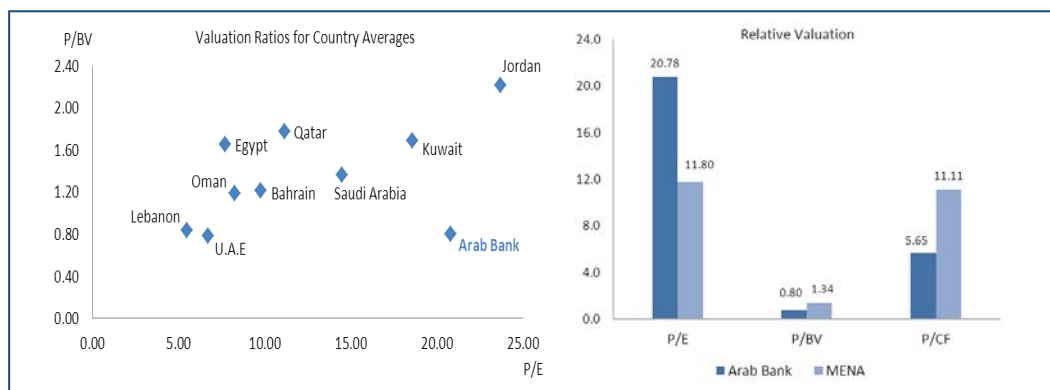
Comparable Firms

The list we compiled consists of 30 of the largest banks that operate in the Middle East. We compared ARBK to the average of those, excluding any banks with under USD 10 billion in assets under management. The largest of the 30 had USD 77.48 billion in assets (Emirates NBD), with the average for the group being just over USD 26 billion. This is compared to ARBK's assets which totaled approximately USD 45.6 billion as of the end of 2011.

The complete list of banks is available in the appendix.

Relative Valuation

When comparing Arab Bank's price-to-earnings ratio (P/E) of 20.78 to the MENA average estimated at 11.8, the Jordanian bank appears to be considerably overvalued. However, a key factor in this analysis that needs to be taken into consideration is the provision that banks have taken over the past year. Arab Bank took provisions worth 1.9% of its loans, almost double the provisions of the MENA average at 1.0% of loans. This has caused its earnings to drop significantly more than the average leading its P/E to appear elevated. When doing a simple scenario taking the mean 1% provision into consideration, Arab Bank's P/E using this adjustment becomes 11.7 which is on par with the MENA average. We can therefore conclude that Arab Bank is fairly valued considering its P/E ratio. The same analysis applies when comparing Arab Bank to the average in Jordan where the P/E for the banking sector is estimated at 13.



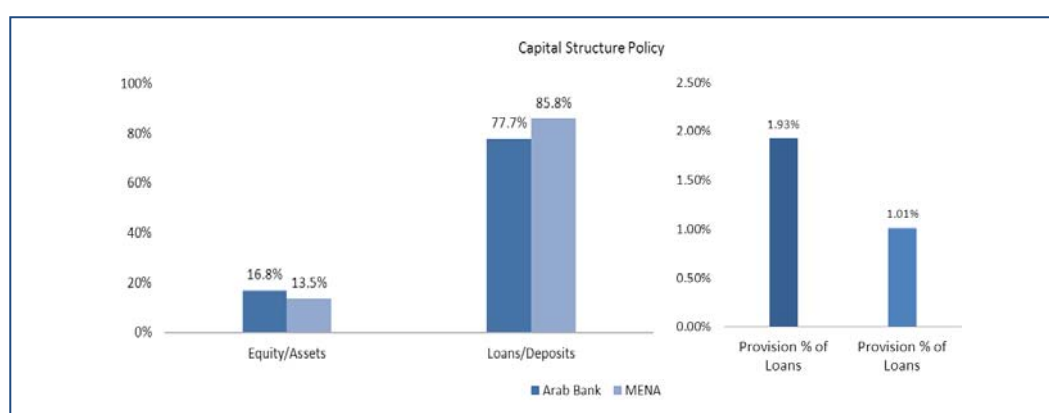
Source: Bloomberg, Reuters

On the other hand, Arab Bank trades at a noticeable discount when looking at price-to-book value (P/BV) or price-to-cash flow (P/CF) ratios. The bank's P/BV is estimated at a mere 0.8 compared to 1.3 for the average, while its P/CF is at 5.7 compared to the peer average at 11.1. Arab Bank's share price has been dropping consistently over the past period, but both its book value and cash flow appear to remain steady causing these ratios to drop considerably. In our opinion, this discount is not only related to the regional upheaval occurring in most Middle Eastern countries where Arab Bank has a tangible presence, but also relates to the recent resignation of Chairman Abdel Hamid Shoman. Once the banking environment in the region improves and the shareholder conflict eases, we believe Arab Bank's share price has room to appreciate and may become an attractive investment. Currently however, we believe its share price accounts the risks associated with the bank.

A country by country breakdown places Arab Banks's relative valuation in the middle of two ends of the spectrum that encapsulates the MENA banking sector. On one end, Egypt, Lebanon and the UAE's banking valuation ratios have them trading at a discount to the average. The political instability in Egypt and Lebanon, along with the economic troubles in Dubai, has caused banking stocks in these countries to trade at a discount relative to the rest of the MENA. On the other end, banks in oil and gas rich countries like Qatar, Saudi Arabia and Kuwait continue to trade at a premium to the MENA averages.

Capital Structure and Policy

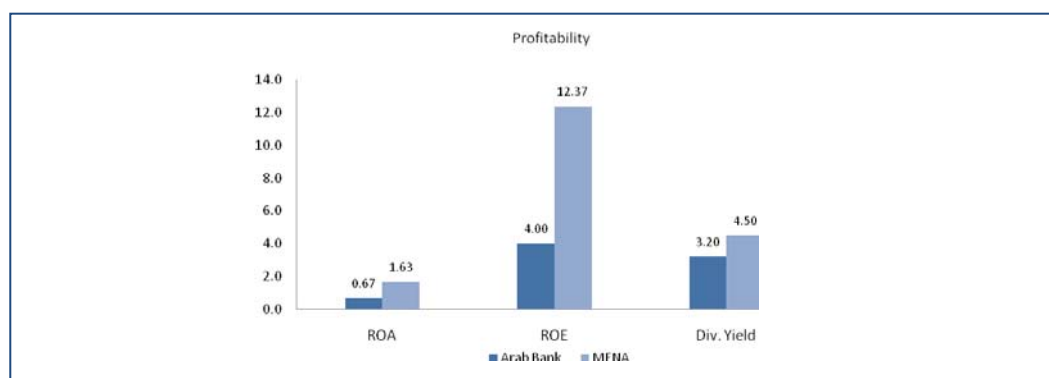
ARBK's equity represents 16.8% of its assets, higher than the 13.5% for the average in the MENA region. When it comes to Loans/Deposits levels, ARBK management's conservative strategy shows as its level stands at 78.5%, versus the MENA average of 85.8% of Loans to Deposits. ARBK's lower levels though have not protected the bank from losses, as its provision to loans ratio is higher than its competitors, at 1.9% vs. 1.0%. These provisions seem to have peaked, but will continue to harm ARBK's bottom line as they gradually decline back to acceptable levels.



Source: Bloomberg, Reuters

Profitability

ARBK's profitability levels have lagged behind its peers, as the higher provisions incurred have led to the steep decline in its earnings. Return-on-assets (ROA) is estimated at around 0.67%, a very weak number compared to MENA banks where the average ROA is 1.63%. Other MENA banks utilize more of customer deposits in the form of loans and enjoy a higher net interest margin spread due to the low cost of funding where depositors require little or no interest, especially in GCC countries. Similarly, ARBK's 2011 return-on-equity (ROE) was a dismal 4.00%, compared to a MENA average of over 12.37%. Even if provisions normalize towards the industry average, ARBK's profitability ratios will still lag the prevalent MENA averages. Dividend yield at ARBK is estimated currently at around 3.2%, also a lower level than its competitors, whom average around 4.50% dividend yield.



Source: Bloomberg, Reuters

VALUATION

We valued ARBK's share at JOD 8.96 using a Dividend Discount Model (DDM) method based on a 5-year forecast with the following assumptions:

Discount Rate

We used a WACC of 12.7% for the purpose of valuing ARBK's equity derived as follows:

$$\begin{aligned} \text{WACC} &= (\text{Weight of Equity} * \text{Cost of Equity}) + (\text{Weight of Debt} * \text{Cost of Debt}) * (1 - \text{Tax Rate}) \\ &= (0.9 * 13.65\%) + (0.1 * 5.0\%) * (1 - 30.0\%) = 12.68\% \end{aligned}$$

$$\begin{aligned} \text{ARBK Cost of Equity} &= \text{Risk-Free Rate} + (\text{Beta} * \text{Market Risk Premium}) \\ &= 8.50\% + (1.14 * 4.50\%) = 13.65\% \end{aligned}$$

- We used a Risk-Free Rate of 8.50% represented by the 5-year Treasury bond recently issued by the Jordanian government. This captures the additional risk of investing in a developing country such as Jordan as opposed to the U.S. Treasury.
- ARBK's beta over the past 10 years is estimated at 1.14. This is a measure of the share volatility against the Amman Stock Exchange, of which Arab Bank share make up nearly 28% of total market capitalization.
- A Market Risk Premium of 4.50% is the result of the difference between the expected return of investing in the Amman Stock Exchange, estimated at 13%, and the Risk-Free Rate of 8.50%. This represents the premium investors expect to gain for realizing the additional risk of investing in securities.

Income Stream Growth Forecasts

As a result of the forecasts for each of the income sources we discussed previously, net income is estimated to grow by over 19% during 2012 followed by similar growth through 2015. We estimate a CAGR of 18.5% for the years between 2012 and 2017.

Income Streams (in USDm)	2011	2012e	2013f	2014f	2015f	2016f	2017f
Net Interest Income	956.8	994.9	1,042	1,121	1,213	1,322	1,444
Net Comm. Income	303.4	326.4	345.1	366.4	390.7	417.4	446.7
Other Revenue	99.3	135.5	151.5	160.6	170.6	181.6	193.7
Profits from Associates	265.9	276.8	292.4	313.3	337.1	365.1	396.2
Total	1,625	1,733	1,831	1,962	2,111	2,286	2,481
Growth in Total Income Streams		6.66%	5.64%	7.14%	7.62%	8.29%	8.53%

Source: BlomInvest

Expectations for Non-Interest Expenses and Loan Impairment Losses / Provisions

We forecast non-interest expenses at around 53% of net revenue (net interest and commissions plus other revenue) guided by ARBK's historicals. As for loan impairment losses and provisions, we expect ARBK to expense slightly less during 2012 than 2011 due to continued improvements in NPLs, with levels maintaining this declining trend afterwards.

In USDm	2011	2012e	2013f	2014f	2015f	2016f	2017f
Operating & Administrative Expenses	722	790	815	873	940	1,018	1,105
Growth (%)	-0.3%	9.5%	3.1%	7.1%	7.6%	8.3%	8.5%
Provisions	434	399	375	324	266	213	152
Provision % of Loans	2.0%	1.8%	1.6%	1.3%	1.0%	0.75%	0.50%

Source: BlomInvest

Calculating Dividends and Share Value

With regards to the cash dividends, Arab Bank follows an established policy of distributing between 20-30% of its share's par value. In 2011, the Board of Directors recommended the distribution of cash dividends of 25%, or JOD 133.5million, compared to 20%, or JOD 106million for the year 2010. We forecast periodic growth in this policy, mirroring expected improvements in earnings and overall performance.

In JODm	2012e	2013f	2014f	2015f	2016f	2017f
Net Income	250	296	361	427	498	578
Payout Ratio (%)	53.5	54.2	44.4	43.7	37.5	36.9
Dividends	133	160	160	186	186	213
PV of Terminal Value	4,019					
PV of Dividends & Terminal Value	4,153	142.2	126.2	130.6	115.9	117.6
Estimated Fair Value (Sum of PV)	4,785					
Outstanding Shares (in millions)	534					
Dividend per Share (in JOD)	0.25	0.30	0.30	0.35	0.35	0.40
Growth (%)	0.0	20.0	0.0	16.7	0.0	14.3
Fair Value per Share (in JOD)	8.96					

Source: BlomInvest

As for the Terminal Growth Rate, we assumed a 5.0% growth rate for dividends beyond 2017. We believe this is an adequate level considering the bank's ability to grow along with the current inflation rates in the region.

Sensitivity Analysis

		Discount Rate				
		10.7%	11.7%	12.7%	13.7%	14.7%
Terminal Growth Rate	4.0%	10.83	9.23	8.03	7.05	6.27
	4.5%	11.64	9.81	8.47	7.38	6.54
	5.0%	12.58	10.48	8.96	7.76	6.83
	5.5%	13.70	11.25	9.52	8.17	7.15
	6.0%	15.06	12.16	10.17	8.65	7.51

Source: BlomInvest

PROJECTED INCOME STATEMENT

<i>USDm</i>	2010	2011	2012e	2013f	2014f	2015f
Interest Income	1,568	1,624	1,690	1,857	2,070	2,312
Interest Expense	635	667	695	814	948	1,099
Net Interest Income	933	957	995	1,042	1,122	1,213
Commission Income	303	322	347	367	390	416
Commission Expense	(17)	(19)	(21)	(22)	(23)	(25)
Net Commission Income	287	303	326	345	366	391
Other Revenue	171	99	143	152	161	171
Net Revenue	1,391	1,359	1,465	1,539	1,649	1,774
Loan Impairment Loss/Provision	(473)	(435)	(400)	(376)	(324)	(266)
Net Revenue After Provisions	917	924	1,065	1,163	1,324	1,508
Non-Interest Expense	(717)	(723)	(791)	(816)	(874)	(940)
Operating Income	199	202	274	347	451	568
Profits from Associates	248	266	278	292	313	337
Pretax Income	447	468	552	640	764	905
Income Tax Expense	(177)	(162)	(182)	(202)	(229)	(272)
Net Income	271	306	370	438	535	634
Minority Interest	(20)	(14)	(18)	(22)	(27)	(32)
Gain from discontinued Operations	-	-	-	-	-	-
Net Income Att. to Shareholders	251	292	351	416	508	602

Source: Arab Bank, BlomInvest

PROJECTED BALANCE SHEET

USDm	2010	2011	2012e	2013f	2014f	2015f
Assets						
Cash and Due from Central Bank	7,645	7,788	8,333	8,811	9,356	9,975
Due from Banks	4,800	4,261	4,322	4,569	4,852	5,175
Direct Credit Facilities	21,347	20,955	22,222	23,497	24,949	26,601
Investments:						
Financial Assets at FVPL	623	953	939	993	1,054	1,124
Financial Assets at FVCI	-	642	632	668	709	756
Other Financial Assets	7,292	7,535	7,448	7,875	8,362	8,915
Total Investments	7,915	9,129	9,028	9,546	10,135	10,807
Investments in Subsidiaries/Associates	2,078	2,245	2,379	2,522	2,699	2,888
Other Assets	1,478	1,236	1,594	1,684	1,784	1,896
Total Assets	45,263	45,613	47,878	50,629	53,775	57,341
Due to Banks	4,950	4,323	4,539	4,721	4,910	5,106
Due to Customers	27,455	28,745	30,182	31,993	34,072	36,457
Cash margin	3,182	2,975	3,065	3,157	3,251	3,349
Borrowed funds	817	810	827	843	860	877
Other liabilities	1,049	1,103	1,236	1,384	1,508	1,603
Total Liabilities	37,453	37,956	39,848	42,098	44,602	47,392
Total Equity (att. to shareholders)	7,648	7,482	7,790	8,278	8,904	9,662
Minority Interest	161	174	239	253	269	287
Total Equity	7,809	7,657	8,030	8,531	9,173	9,948
Total Liabilities & Equity	45,263	45,613	47,878	50,629	53,775	57,341

Source: Arab Bank, BlomInvest

APPENDIX

I – List of Comparable Peers

Company	Country	Total Assets	Capital Structure and Policy			Valuation Ratios			Profitability		
			Equity / Assets	Loans / Deposits	Provision % of Loans	P/E	P/BV	P/CF	ROA	ROE	Dividend Yield %
AHLI UNITED BANK B.S.C	BAHRAIN	28,330	10.3%	92.5%	0.81%	9.74	1.21	7.96	1.13	12.60	4.84
COMMERCIAL INTERNATIONAL BAN	EGYPT	14,182	10.3%	58.1%	0.78%	7.64	1.68	8.92	2.01	18.66	4.28
NATIONAL SOCIETE GENERAL	EGYPT	10,372	13.1%	70.2%	0.38%	7.76	1.62	7.26	2.41	21.28	4.40
HOUSING BANK FOR TRADE AND	JORDAN	9,786	15.1%	55.1%	1.74%	23.67	2.21	18.46	1.29	9.45	3.03
KUWAIT FINANCE HOUSE	KUWAIT	48,345	15.4%	16.6%	-	25.75	1.08	17.70	0.62	4.48	1.98
GULF BANK	KUWAIT	17,190	9.0%	106.0%	1.94%	37.54	2.42	33.09	0.65	7.28	-
COMMERCIAL BANK OF KUWAIT	KUWAIT	13,341	14.3%	102.2%	4.39%	-	1.86	-	0.02	0.16	-
AL AHLI BANK OF KUWAIT	KUWAIT	11,062	15.9%	-	-	18.46	1.73	19.85	1.67	10.49	2.55
BURGAN BANK	KUWAIT	16,349	12.4%	84.0%	1.25%	11.14	1.37	10.32	1.16	11.65	2.27
BANK AUDI SAL - AUDI SARADAR	LEBANON	28,775	8.2%	35.6%	-0.62%	6.00	0.83	10.52	1.26	15.80	6.97
BLOM BANK	LEBANON	23,165	8.6%	47.8%	0.41%	4.92	0.84	5.03	1.42	17.40	6.06
BANKMUSCAT SAOG	OMAN	18,774	12.0%	105.2%	0.67%	8.26	1.19	8.00	1.80	14.11	3.82
MASRAF AL RAYAN	QATAR	15,180	15.4%	78.2%	0.24%	14.10	2.38	14.12	3.13	18.02	1.86
QATAR ISLAMIC BANK	QATAR	16,008	22.0%	108.1%	0.65%	12.42	1.71	13.11	2.48	13.48	5.88
COMMERCIAL BANK OF QATAR QSC	QATAR	19,648	19.9%	107.7%	0.57%	8.99	1.29	9.64	2.81	14.10	8.70
DOHA BANK QSC	QATAR	14,397	13.5%	98.5%	0.82%	9.02	1.74	8.75	2.49	18.93	8.12
RIYAD BANK	SAUDI ARABIA	48,234	16.7%	82.2%	0.58%	10.45	1.14	10.17	1.78	10.61	6.51
SAUDI BRITISH BANK	SAUDI ARABIA	36,973	12.4%	82.3%	0.55%	11.37	1.92	11.13	2.19	17.86	1.43
BANQUE SAUDI FRANSI	SAUDI ARABIA	37,459	14.0%	85.4%	0.17%	10.85	1.49	9.82	2.21	15.46	3.30
ARAB NATIONAL BANK	SAUDI ARABIA	31,351	14.2%	85.9%	0.82%	10.40	1.40	9.53	1.86	13.61	3.65
ALINMA BANK	SAUDI ARABIA	9,808	43.2%	142.8%	0.49%	36.25	1.16	35.54	1.36	2.74	-
SAUDI HOLLANDI BANK	SAUDI ARABIA	15,346	12.9%	86.2%	0.41%	9.89	1.46	9.42	1.85	14.96	3.09
SAUDI INVESTMENT BANK	SAUDI ARABIA	13,851	16.5%	79.8%	0.98%	12.25	1.01	12.71	1.37	8.49	3.15
NATIONAL BANK OF ABU DHABI	UAE	69,603	10.3%	108.2%	0.91%	8.52	1.20	8.27	1.59	14.68	2.65
FIRST GULF BANK	UAE	42,873	17.0%	104.7%	1.43%	6.17	0.89	6.75	2.49	14.60	6.44
ABU DHABI COMMERCIAL BANK	UAE	50,018	12.0%	118.7%	1.60%	5.73	0.81	5.88	1.67	16.08	5.99
EMIRATES NBD PJSC	UAE	77,484	12.3%	111.4%	2.31%	8.78	0.45	5.08	0.89	7.38	7.19
DUBAI ISLAMIC BANK	UAE	24,662	11.2%	90.7%	1.85%	7.02	0.81	6.10	1.12	10.94	6.54
ABU DHABI ISLAMIC BANK	UAE	20,237	11.5%	46.4%	3.21%	6.22	0.81	5.87	1.54	13.85	7.98
UNION NATIONAL BANK/ABU DHAB	UAE	22,451	15.8%	98.2%	1.00%	4.59	0.54	4.41	0.59	1.84	12.20

Source: Bloomberg, Reuters

II – Comparable Average by Country

Company	Total Assets	Capital Structure and Policy			Valuation Ratios			Profitability		
		Equity / Assets	Loans / Deposits	Provision % of Loans	P/E	P/BV	P/CF	ROA	ROE	Dividend Yield %
MENA AVERAGES	26,842	14.5%	85.8%	1.01%	11.80	1.34	11.11	1.63	12.37	4.50
ARAB BANK	45,613	16.8%	78.5%	1.93%	20.78	0.77	5.65	0.67	4.00	3.20
<u>Averages by Country</u>										
BAHRAIN	28,330	10.3%	92.5%	0.81%	9.74	1.21	7.96	1.13	12.60	4.84
EGYPT	12,277	11.7%	64.1%	0.58%	7.70	1.65	8.09	2.21	19.97	4.34
JORDAN	9,786	15.1%	55.1%	1.74%	23.67	2.21	18.46	1.29	9.45	3.03
KUWAIT	21,258	13.4%	61.8%	1.52%	18.58	1.69	16.19	0.82	6.81	1.36
LEBANON	25,970	8.4%	41.7%	-0.11%	5.46	0.84	7.78	1.34	16.60	6.52
OMAN	18,774	12.0%	105.2%	0.67%	8.26	1.19	8.00	1.80	14.11	3.82
QATAR	16,309	17.7%	98.1%	0.57%	11.13	1.78	11.41	2.73	16.13	6.14
SAUDI ARABIA	27,575	18.5%	92.1%	0.57%	14.49	1.37	14.05	1.80	11.96	3.02
UAE	43,904	12.9%	96.9%	1.76%	6.72	0.79	6.05	1.41	11.34	7.00

Source: Bloomberg, Reuters

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Recommendations are based on the upside (downside) between our 12-month Fair Value estimate and the current Market Price.

Buy: Fair Value higher than Market Price by at least 20%

Accumulate: Fair Value higher than Market Price by 10% to 20%

Hold: Fair Value ranges between -5% to +10% in relation to Market Price

Reduce: Fair Value lower than Market Price by 5% to 15%

Sell: Fair Value lower than Market Price by at least 15%

Risks are based on share price volatility along with qualitative factors such as the nature of the business, the country risk and sensitivity to a single event, single product or single buyer. We've arranged the risk factor into 5 trenches:

- High Risk
- Medium-to-High Risk
- Medium Risk (similar to Market Risk)
- Medium-to-Low Risk
- Low Risk

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