

Day Break

Tuesday, 06 June 2017

COMPANY UPDATE

UNITED BANK LIMITED

COMMERCIAL BANKS

Recommendation	BUY
Target Price:	275.2
Last Closing: 5-Jun-17	233.8
Upside:	17.7
Valuation Methodology:	Asset based Valuation / Dividend Discount Model (DDM)
Time Horizon:	Dec-17

Market Data

Bloomberg Tkr.	UBL PA
Shares (mn)	1,224.2
Free Float Shares (mn)	489.7
Free Float Shares (%)	40.0%
Market Cap (PKRbn USDmn)	286.2 2,731.2
Exchange	KSE 100
Price Info.	90D 180D 365D
Abs. Return	(6.0) 6.1 35.6
Lo	222.7 220.3 164.4
Hi	275.4 275.4 275.4

Key Company Financials

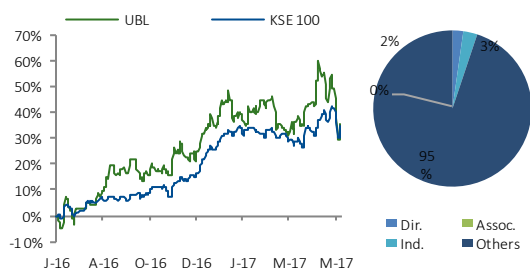
Period End: Dec

PKRbn	CY16A	CY17E	CY18F	CY19F
Total Revenue	77.8	80.7	77.5	85.3
Net Income	25.73	27.7	24.8	29.8
EPS (PKR)	21.0	22.7	20.2	24.3
DPS (PKR)	13.5	13.0	11.0	13.0
Total Assets	1,400.7	1,577.6	1,736.5	1,960.0
Total Equity	142.1	151.8	163.1	177.0

Key Financial Ratios

ROE (%)	18.1	18.3	15.2	16.8
P/E (x)	11.1	10.3	11.6	9.6
P/B (x)	2.0	1.9	1.8	1.6
DY (%)	5.8	5.6	4.7	5.6

Relative Price Performance & Shareholding



About the Company

The Bank was incorporated in Pakistan and is engaged in commercial banking and related services. The Bank is a subsidiary of Bestway (Holdings) Limited which is incorporated in UK and listed on LSE Professional Securities Market.

Source: Bloomberg, KSE 100 & IGI Research

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Commercial Banks

UBL; Recent Sell-off makes it an attractive Buy

- UBL reported profits of PKR 2.8bn (or PKR 1.75/share) in 1QCY17, down by a meagre 0.6%YoY; compared to big 5 banks (ex-UBL) profitability down by 6%.
- Key driver for net interest income was the reduction in bank's cost of deposit to 2.7% (2.8% in 1QCY16) despite a +11%YoY increase in deposits (~17% industry deposit growth).
- Bank's net advances increased by +12%; but lowered lending rate reduced banks average earning yield on advance to 6.4% from 7.5% recorded in CY16.
- IDR increased to 73%, accompanied by drop in investment yields from +8.9% in FY16 to +8.3% in 1QFY17 as banks substituted maturing PIBs with T-bills.
- Looking ahead, we highlight UBL as the best growth bet amongst banking sector based on bank's sound fundamentals and adequate asset/capital structure; ideally place to encapsulate country's growth outlook.

UBL stock down by 14% in recent MSCI sell-off

United Bank Limited (UBL), one of the largest banks in Pakistan, has had a dismal week in wake of inclusion in MSCI Emerging Markets index. The stock came down by nearly 14.4% to date, since formal announcement (16th May, 2017) of Pakistan inclusion in MSCI Emerging Market Index; compared to market return of negative 6%. However, given the bank's performance and the undervalued status, we see an opportunity for investors to get a piece of UBL profits.

Steady profit growth display in 1QCY17

To recall, UBL reported profits of PKR 2.8bn (or PKR 1.75/share) in 1QCY17, down by a meagre 0.6%YoY; compared to big 5 banks (ex-UBL) profitability down by 6%. Bank's net interest income rose by a meagre +1%YoY to PKR 13.7bn, wherein net interest margins compressed from 4.4% recorded in CY16 to 3.9% (down by 50bps) in 1QFY17, which is consistent with the banking sector as a result of low interest rate environment. Key driver for net interest income was the reduction in bank's cost of deposit to 2.7% (2.8% in 1QCY16) despite a +11%YoY increase in deposits (~17% industry deposit growth), sustained net advances growth of +12%YoY (with yield on performing advances averaging 6.4%) and +10%YoY increase in net investments (with yield averaging 8.3%).

Asset mix skewed to investments...

In terms of asset mix, UBL increased its investment by +7% bringing investment-to-deposit Ratio (IDR) to 73%. However, this was accompanied by drop in investment yields from +8.9% in FY16 to +8.3% in 1QFY17 as banks substituted maturing Pakistan Investment Bonds (PIBs) with treasury bills; for UBL, investment in T-bills almost doubled to PKR 193bn (with average yield of 5.9% in 1QCY17) from PKR 109bn recorded in 4QCY16.

Exhibit: UBL Investment yield

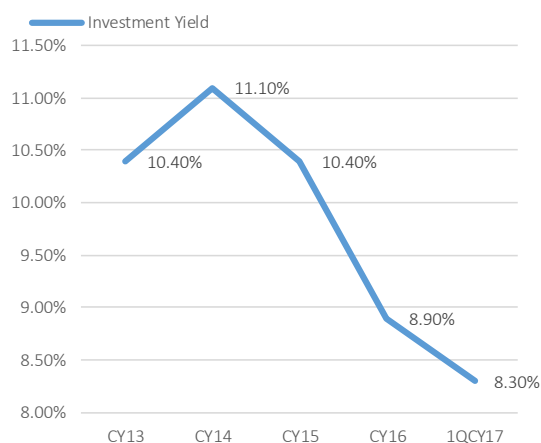


Exhibit: UBL Investment Concentration

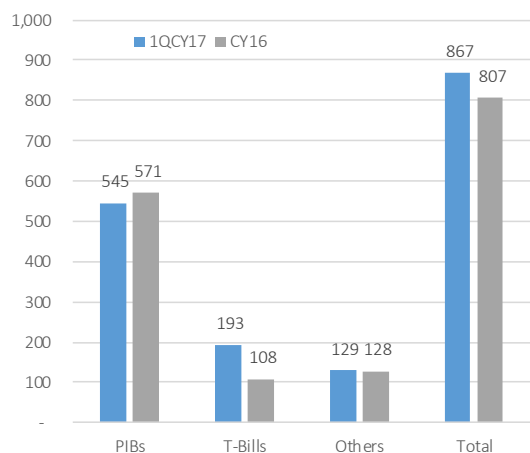
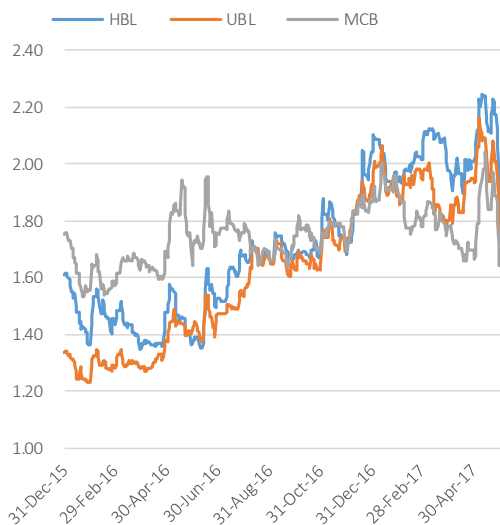


Exhibit: Large bank P/B movement



Despite a healthy +12% growth witnessed in net advances

Bank's net advances increased by +12%; but lowered lending rate reduced banks average earning yield on advance to 6.4% from 7.5% recorded in CY16. However, the increase in advances had little effect on bank's asset quality, whereby Non-performing Loans (NPLs) of the bank further came down to PKR 44.5bn, (down by 6%YoY) bringing bank's infection ratio to 8.3% with increasing coverage ratio at 91.4%. Resultantly, provisioning expense has come down from PKR 1.6bn in 1QFY16 to mere PKR 29mn in 1QFY17.

Lower capital gain and fee income depressed overall non-interest come; compensated by lower operating expense

However, disappointingly bank's non-Interest income declined by -25%YoY to PKR 6.3bn, led by -32% fall in capital gains and dividend income. Excluding treasury income non-interest income down by a massive 17% owing to 12% decline in fee income (lower remittances and trade commissions). On the cost side, operating expenses slid to PKR 8.7bn, down by -2%YoY even though the administrative expenses grew by a meagre +1%YoY; which given decline in total revenue, cost-to-income increased to +44% compared to +41% in the same period last year.

Exhibit:

UBL Result Highlights

PKRmn (Period end=Dec)	1QCY17	1QCY16	YoY	4QCY16	QoQ
Interest Earned	23,888	23,423	2%	24,864	-4%
Interest Expensed	10,176	9,837	3%	10,820	-6%
Interest Income	13,712	13,587	1%	14,044	-2%
Fee Income	2,787	3,175	-12%	3,174	-12%
Capital Gain & Div. Income	2,887	4,266	-32%	1,446	100%
Non-Interest Income	6,276	8,360	-25%	5,191	21%
Total Revenue	19,988	21,947	-9%	19,235	4%
Operating Expenses	8,736	8,923	-2%	8,451	3%
Pre-Provisioning Profits	11,251	13,023	-14%	10,785	4%
NPL (Rev.) / Prov.	96	1,768	n.m.	349	-73%
Pre-Tax Profits	11,156	11,256	-1%	10,435	7%
Taxation	3,901	3,956	-1%	4,010	-3%
Profit After Tax	7,255	7,300	-1%	6,426	13%

EPS (PKR)	5.93	5.96	5.25
DPS (PKR)	3.00	3.00	4.00
BVPS (PKR)	125.93	119.24	123.99

KEY RATIOS

Cost-To-Income Ratio	44%	41%	44%
Effective Tax Rate	35%	35%	38%
Non-II / Total Income	31%	38%	27%

SOURCE: IGI Research, Company accounts, PSX notifications

Recommendation

Looking ahead, we highlight UBL as the best growth bet amongst banking sector based on bank's sound fundamentals and adequate asset/capital structure; ideally place to encapsulate country's growth outlook. The bank is trading at an attractive forward P/B (ROE) of 1.9x (18.3%) compared to HBL and MCB with 2.0x (17.4%) and 1.7x (+15.5%). We recommend a 'Buy' rating on UBL with Dec-17 target price of PKR 275/share indicating +18% upside from yesterday's closing price; combined with a dividend yield of 5.6% bank offer total return of +23%.

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Recommendation	Rating System
Buy	If target price on aforementioned security(ies) is more than 10%, from its last closing price(s)
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Time Horizon: Dec - 2017

Valuation Methodology: The analyst(s) has used following valuation methodology to arrive at the target price of the said security (ies):

DDM (Dividend Discount Model)

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