Day Break

Wednesday, 01 August 2018

Commercial Banks

Exhibit: Banks Valuation Matrix

	2018 PER (x)	2018 PB (x)	2018 DY (%)	Target Price (Dec2018)
HBL	9.4	1.3	4.5	162.6
UBL	9.5	1.3	6.3	190.9
MCB	8.5	1.6	9.9	232.8
ABL	9.2	1.1	5.9	108.1
NBP	4.6	0.6	8.0	66.2
BAFL	9.2	1.3	5.3	55.2
BAHL	11.4	1.9	4.4	89.8
FABL	7.1	0.9	4.4	34.9
AKBL	5.1	0.8	6.0	40.9
HMB	9.0	1.0	7.1	41.7

Exhibit: Banks Qtrly Profitability

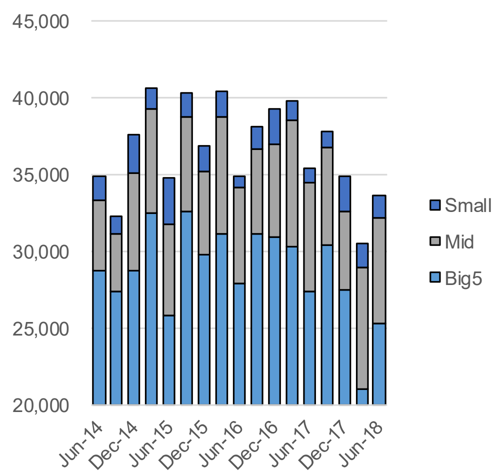
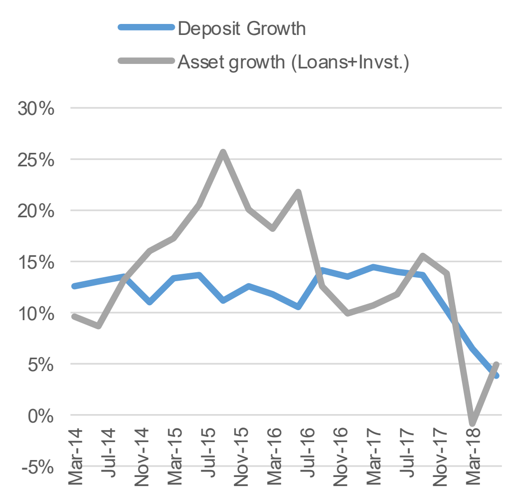


Exhibit: Banks Balance sheet Growth



Source: SBP,Company Accounts, IGI Research

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Commercial Banks

Rate Hike to Benefit Banks' Interest Income; But More Likely to Feel the Pain elsewhere

- We preview 2QCY18 banking sector earning result. We expect profitability to decline by ~5%YoY to PKR 33.6bn, whereby big5 banks profitability is expected to be worst hit.
- Banks had a patchy start to the year. During the 1QCY18, asset growth has been slowest in the past ~4yrs while deposits keep piling on. A combination which led to weakest profitability display.
- Interest income along with fee income is expected to grow modestly, however, lower capital gains on fixed income bonds will keep overall non-interest growth restricted.
- A big positive impact is expected to come from loan loss provisions, however, investments are likely to suffer from a less buoyant capital markets performance and higher effective tax rate owing to super-tax will keep profitability rather slim.
- Amongst our coverage banks, we have strong preference for MCB, FABL and AKBL.

Banks earning preview

We preview 2QCY18 banking sector earning result. We expect profitability to decline by ~5%YoY to PKR 33.6bn, whereby big 5 banks' profitability is expected to get worst hit.

Exhibit:

Expected 2QCY18 banks financial Highlights

PKRmn	2QCY18e	2QCY17	YoY	QoQ	1HCY18	1HCY17	YoY
Net Interest Income	94.9	93.5	2%	2%	187.9	181.5	4%
Fee Income	21.7	20.5	6%	7%	42.1	38.7	9%
Non-Interest Income	37.6	40.1	-6%	7%	72.9	78.5	-7%
Total Revenue	132.5	133.6	-1%	4%	260.8	260.0	0%
Operating Expenses	74.8	70.9	6%	3%	147.5	137.1	8%
Pre-Provisioning Profits	57.8	62.7	-8%	4%	113.3	122.9	-8%
Provision (Rev.) / Charge	(0.5)	0.9	n.m.	-40%	(1.3)	(0.6)	1.15x
Pre-Tax Profits	58.2	61.8	-6%	22%	105.8	123.5	-14%
Taxation	24.6	26.4	-7%	44%	41.7	48.2	-13%
Profit After Tax	33.6	35.4	-5%	10%	64.1	75.3	-15%

Source: Company Financials, IGI Research

Patchy Start to CY18; Weakest Profitability Display in 1Q

Banks had a patchy start to the year. During the 1QCY18, asset growth has been slowest in the past ~4yrs while deposits kept piling on. A combination which led to weakest profitability display. Adjusted to one-offs, big 5 banks were the worst performer with profitability down by nearly 31%YoY. For 2QCY18, we do not expect banks earning seasons to be eventful. Asset growth has picked up pace ahead of deposit growth, which will provide some relief to shrinking NIMs. However, banks are more likely to feel the pain elsewhere. Higher taxation, lower non-funded income and bearish market performance will bulge up more provisions under investments.

Rate Hike to Benefit Banks Interest Income; But More Likely to Feel the Pain Elsewhere

Interest income along with fee income is expected to grow modestly just over +2%YoY, however lower capital gains on fixed income bonds will keep overall non-interest growth restricted despite seeing a +6%YoY growth in fee income. Thus total revenue is likely to show a decline of 1%YoY during 2QCY18. Amongst our coverage banks, MCB and FABL are most likely to show a growth in revenues, led by higher interest income growth (average of ~10%YoY). Banks across are also likely to face higher operating expenses, with HBL leading the chart as it continues to book expenses related to NY branch ongoing compliance transformation program. A bigger positive impact is expected to come from loan loss provisions. Expect UBL (due to its international branches) nearly all banks have been reporting net reversals. However, investments are likely to suffer from a less buoyant capital markets performance in 2QCY18, which will keep overall provisioning charge supportive rather than limited. Finally, we expect higher effective tax rate owing to super-tax charge.

Exhibit:

Expected 2QCY18 banks EPS (DPS)

PKR	2QCY18e	2QCY18e (DPS)	2QCY17	2QCY17 (DPS)	YoY	QoQ	1HCY18e	1HCY18e (DPS)	1HCY17	1HCY17 (DPS)	YoY
HBL	4.1	1.00	4.4	3.5	-7%	31%	7.2	2.00	10.6	7.00	-32%
UBL	4.5	3.00	4.9	3.0	-9%	1.06x	6.6	6.00	10.8	6.00	-39%
MCB	4.5	4.00	6.4	4.0	-29%	12%	8.5	8.00	11.6	8.00	-26%
ABL	2.8	1.75	2.5	1.8	12%	-15%	6.1	3.50	5.7	3.50	8%
NBP	2.5	-	2.0	-	22%	5%	4.9	-	4.0	-	21%
BAFL	1.4	-	1.3	-	7%	-31%	3.4	-	3.0	-	13%
BAHL	1.9	-	2.0	-	-6%	1%	3.8	-	4.2	-	-9%
FABL	0.7	-	0.7	-	15%	-6%	1.5	-	1.9	-	-18%
AKBL	1.1	-	1.4	-	-23%	0%	2.2	-	2.4	-	-9%
HMB	1.0	-	0.9	-	45%	-12%	2.5	-	2.1	-	32%

Source: Company Financials, IGI Research

Recommendation

We maintain an overweight stance on sector eyeing further rate hike of 50bps by 2019 end. Amongst our coverage banks, we have strong preference for MCB, FABL and AKBL.

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