

PAKISTAN BANKS

MARKET VISTA

MEBL: Inherent immunities make for Buy

- We roll over our TP for Meezan Bank Limited (MEBL) to Dec'21 to stand at Pkr137.0/sh (Previously: Pkr100.0/sh) offering an upside of 36.2% from last close. The stock is currently trading at a CY21F P/B of 1.7x vs. industry's P/B of 0.8x where we believe premium valuations are justified given bank's higher ROE generation (CY21-23F ROE: 28.5%) vis-à-vis industry's ROE of 14.0%.
- MEBL due to its inherent positioning in the banking space is in a sweet-spot, poised to capitalize on macro opportunities where, i) the bank stands most sensitive to interest rates that are likely to uptrend (Dec'21-end policy rate expected at 8.5%), ii) increase in financing demand aided by TERF and housing finance (3y CAGR est. at 20.7%), and iii) prudent risk management (coverage ratio maintained at 140.1% in Sep'20).
- Additional triggers could come from potential circular debt liquidity injections (with quantum, timing yet to be finalized) through Sukuk issuance and Govt. continuing to channel borrowings from Islamic banking space.
- MEBL continues to broaden its foot print in retail market with addition of 42 more branches (c. increase in past 2y: 142 branches, 17.7% of total branch network) – a trend likely to continue in the medium run – assisting in maintaining deposit growth at 20.5% avg. over the same period and multiplying the gains from interest rate hikes.

Inherent advantages of MEBL to get more prominent: MEBL with its interest rate sensitive assets/interest rate sensitive liabilities standing at 1.5x as of Sep'20, highest in the industry, is poised to gain from interest rate hikes which are expected to begin from May'21 (Dec'21-end policy rate expected at 8.5%). Moreover, increase in financing demand aided by TERF and housing finance (3y CAGR est. at 20.7%), bank managing to hold its delta on saving accounts despite sharp cut in interest rates (Nov'20: 2.23ppts vs. 2.05ppts in Apr'20) acting as test-case for passing-on interest rate hikes, and prudent risk management (coverage ratio maintained at 140.1% in Sep'20, though cost of provisioning conservatively assumed at avg. 0.65% for CY21-23) are other attributes benefitting MEBL earnings in the medium run. Certain regulatory waivers (IBFT charges etc.) have negatively impacted MEBL (3.3x YoY increase in app transaction volumes in 1HCY20), however we have incorporated restoration of charges (fee income 3y CAGR: 13.2%). As such, CY20-23F earnings CAGR stands at 13.1% attributable to stronger growth in the medium run. Additional trigger to earnings could come from potential (but limited) circular debt repayment through Sukuk issuance.

Branch expansion continues; NIMs to stand at ~5% in the med-to-long run: MEBL continues to broaden its foot print in retail market with addition of 42 more branches (c. increase in past 2y: 142 branches, 17.7% of total branch network) – a trend likely to continue in the medium run – assisting in maintaining deposit growth at 20.5% avg. over the same period. This should multiply the gains from hike in interest rates even assuming normalization in delta on saving accounts (differential between interest bearing deposits of MEBL vs. conventional banks to gradually decline to 1.5% vs. 2.5% of CY20F) with NIMs at close to 5% over medium to long run vs. last 5y NIMs of 4.42%. Consequently, net interest income is likely to grow at a 3y CAGR of 12.6% despite flattish NII expected next year due to high base effect (Short term repricing mismatch has mainly augmented NII by 50.0%YoY during 9MCY20).

Investment perspective: MEBL has gained 50.1% during the past six months to trade at a CY21F P/B of 1.7x vs. industry P/B of 0.8x. We believe premium valuations are justified given higher ROE generation (CY21-23F ROE: 28.5%) vis-à-vis industry's ROE of 14.0%. Our Dec'21TP for the stock stands at Pkr137/sh offering an upside of 36.2%. While dividend yield has not been exciting of the bank (CY21F dividend yield: 8.0%), we believe MEBL with its CET-1 capital standing at 16.1% could provide surprise on its payout going forward.

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BUY

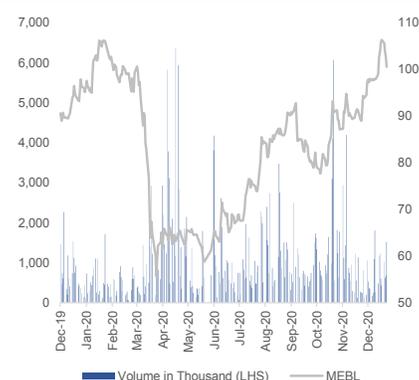
TARGET PRICE (Pkr)	SHARE PRICE (Pkr)
137.0	100.57
UPSIDE/DOWNSIDE	DIV. YIELD
36.2%	8.0%

MEBL: Valuation Glance

	CY19A	CY20F	CY21F	CY22F
EPS (Pkr)	12.1	15.9	14.9	16.6
DPS (Pkr)	4.0	8.0	8.0	8.0
BVPS (Pkr)	48.8	52.7	59.2	67.5
P/E(x)	8.3	6.3	6.8	6.1
P/BV(x)	2.1	1.9	1.7	1.5
Div.Yield	4.0%	8.0%	8.0%	8.0%
Earn. Growth	73.0%	45.0%	-6.0%	12.0%
ROA	1.4%	1.7%	1.3%	1.2%
ROE	29.7%	33.2%	26.9%	26.6%

Source: Company reports & AKD Research

MEBL: Price vs Volume



Source: PSX & AKD Research



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Valuation Methodology

To arrive at our period end target prices, AKDS uses different valuation techniques including:

- Discounted Cash Flow (DCF, DDM)
- Relative Valuation (P/E, P/B, P/S etc.)
- Equity & Asset return based methodologies (EVA, Residual Income etc.)

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Buy	> 14.5% expected total return (Rf: 8.5% + Rp: 6%)
Neutral	> 8.5% to < 14.5% expected total return
Sell	< 8.5% expected total return (Rf: 8.5%)



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