



AKD Securities Limited

TREC Holder & Registered Broker
Pakistan Stock Exchange

Equity Research / Pakistan



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Today's Daily

■ Pakistan Banks: Sector update

Latest banking sector data for Apr'17 indicates that banks' earning assets continue to grow at strong levels (+9%YoY) to PkR12.3tn. While banks continue to maintain their preference for risk-free GoP securities (investments up 12%YoY while almost remaining flat since Jun'16), a healthy 15.7%YoY growth in private sector credit is encouraging. In this regard, while conventional heavy borrowers, Textiles and Food sector topped the list of sectors attracting the most credit, we see a promising 27%YoY uptick in borrowings by the Construction sector. This we believe, is CPEC infused largely, with players gearing up for higher infrastructure development in the upcoming years (expansions totaling 26.9mtpa in the Cement listed space). Consumer financing grew by a healthy 16.8%YoY in Apr'17 (8.3% of the private sector loans) as banks look to re-focus on high margin auto finance and personal loans in the current lower inflationary environment. Expecting spreads to bottom out this year with reversal likely in Nov'17, we retain our liking for banks that have: 1) the room to benefit from loan growth, 2) an adequate CAR buffer, 3) achieved economies of scale and 4) a strong non-interest income franchise. Playing this theme, we like HBL and UBL, where the recent bearish spell (down 7%/10% MoM) has opened up valuations.

KSE100 - Index

Current 50,162.81
Previous 50,144.63
Chg. 0.04%

Mkt Cap. (PkRbn/US\$b)

Current 9,960 / 94.99
Previous 9,939 / 94.79
Chg. 0.21%

Daily Turnover (mn)

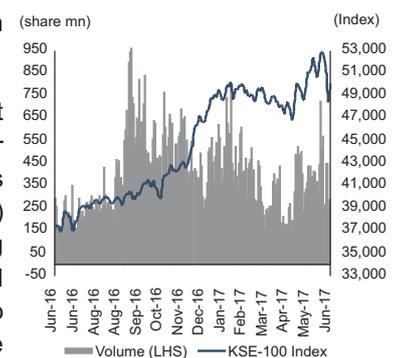
Current 232.51
Previous 231.74
Chg. 0.3%

Value Traded (PkRmn/US\$m)

Current 11,324 / 108.00
Previous 13,543 / 129.17
Chg. -16.4%

News and Views

- The Supreme Court (SC) has expressed satisfaction over the second 15-day progress report submitted by the JIT, investigating the Panama leaks case. While asking an explanation from JIT over Hussain Nawaz's leak photograph, SC has made clear that there would be no extension in the investigation time-frame (initially set at 60 days).
- The ECC in its meeting presided by FM Ishaq Dar has approved: 1) not to deregulate the price of sugarcane, 2) extension of the deadline for export of sugar up to Jul 31'17, 3) payment of salaries to the employees of Pakistan Steel Mills Corporation (PSMC) for the month of Feb'17, 4) provision of bridge financing of PkR864mn for facilitating the Printing Corporation of Pakistan, 5) allocation of 10 MMCFD gas from Tolanj field to SNGPL, 6) allocation of 2.9 MMCFD gas from Khamiso-01 well to EFERT and 7) government guarantee for a syndicated term finance facility of PkR41bn for the power sector.
- The KPK gov't has unveiled PkR603bn budget for FY18 comprising development outlay of PkR208bn with major focus on elimination of corruption and development of the social sector besides announcing 10% increase in the salaries and pension of the gov't employees after merger of 2010 ad-hoc relief.



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Pakistan Banks: Sector update

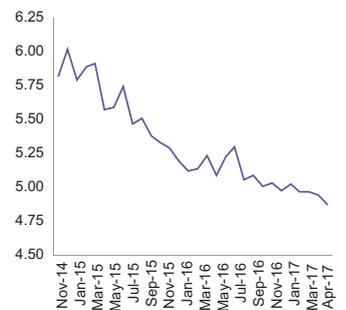
Latest banking sector data for Apr'17 indicates that banks' earning assets continue to grow at strong levels (+9%YoY) to PkR12.3tn. While banks continue to maintain their preference for risk-free GoP securities (investments up 12%YoY while almost remaining flat since Jun'16), a healthy 15.7%YoY growth in private sector credit is encouraging. In this regard, while conventional heavy borrowers, Textiles and Food sector topped the list of sectors attracting the most credit, we see a promising 27%YoY uptick in borrowings by the Construction sector. This we believe, is CPEC infused largely, with players gearing up for higher infrastructure development in the upcoming years (expansions totaling 26.9mtpa in the Cement listed space). Consumer financing grew by a healthy 16.8%YoY in Apr'17 (8.3% of the private sector loans) as banks look to re-focus on high margin auto finance and personal loans in the current lower inflationary environment. Expecting spreads to bottom out this year with reversal likely in Nov'17, we retain our liking for banks that have: 1) the room to benefit from loan growth, 2) an adequate CAR buffer, 3) achieved economies of scale and 4) a strong non-interest income franchise. Playing this theme, we like HBL and UBL, where the recent bearish spell (down 7%/10% MoM) has opened up valuations.

Spreads remain under 5%: With 4MCY17 spreads registering at an average 4.94%, weighted average banking sector spreads clocked in at 4.87% for Apr'17, lower by 22bpsYoY/ 7bpsMoM. The downtrend in spreads is more on account of a 57bps drop in lending yields to 7.85% against 35bps decline in deposit costs to 2.98% on a YoY basis. We believe, spreads are likely to continue trending in the 4.8%-5.0% range for the remainder of the year where a 25bps increase expected in Nov'17 is unlikely to do any good. That said, we will see a more visible improvement beyond CY17F with spreads averaging in the range of 6.0-6.5% in the medium term.

Private sector growth shows an encouraging trend: Despite risk-free government securities continuing to be the banking sector's preference, a healthy 15.8%YoY growth in private sector credit as of Apr'17 has been encouraging. While selected sectors like Textiles, Foods and Electricity have been the key recipients of industry's credit disbursements (making up 44% of the total private sector loans), we see the 27%YoY uptick in borrowings by the Construction sector as promising.

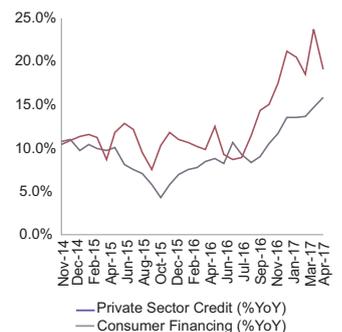
Consumer financing continues to expand: Consumer financing grew by a healthy 19.1%YoY in Apr'17, making up 8.3% of the private sector loans in Apr'17, as banks look to re-focus on high margin auto finance and personal loans in the current lower inflationary environment. Going forward, while interest rates are poised to go up, they are still likely to remain in mid-single digit keeping room available for continued growth in advances.

Banking Spreads



Source: Company Report & AKD Research

Pvt Sector credit growth on an uptick



Source: Company Report & AKD Research



Investment perspective: With interest rates likely to bottom out this year, we retain our liking for banks that have: 1) the room to benefit from CPEC led loan growth, 2) an adequate CAR buffer, 3) achieved economies of scale and 4) a strong non-interest income franchise. Playing this theme, our preferred plays include HBL (TP: PKR296.1/sh, upside: 9.4%) and UBL (TP: PKR270.1/sh, upside: 14.9%). In addition to the aforementioned factors, potential multiple expansion on account of inclusion into MSCI EM (AKD Banking Universe trades at a 24% discount to banks in MSCI EM space), can provide further upside.



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Neutral	≤ 5% to ≥ -5% potential
Reduce	< -5% to > -20% downside potential
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