AKD Daily

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Today's Daily

MCB: The right mix of growth and value

Asset quality deterioration and increase in expenses characterized MCB's earnings performance in CY17. This, we believe was more a consequence of NIB acquisition with the bank inheriting PkR29bn additional infected loans while cost inefficiencies were a function of the bank's small size. Impairment charge during the year was another drag on earnings with the bank booking provisions worth PkR3.5bn - highest ever as the benchmark index lost 15% during the year. That being said, the bank is encouragingly focusing on: 1) building its loan book (17%YoY growth in advances ex-NIB) particularly in the consumer space, 2) targeting CA growth to support NIMs alongwith concentration towards the shorter end of maturity profile to benefit from DR upcycle and 3) increasing its fee income base (+22%YoY). While earnings will rebound from CY18F, improvements on the cost front (C/I ratio to go down to 44% by CY19F from 51% in CY17) and provision (NPL ratio to gradually come down to 6% by CY19F) should become more visible by CY19F. MCB has gained 6% CYTD to trade at a forward PB/PER of 1.5x/11.0x where superior earnings growth (3yr NPAT CAGR of 13%) and strong management credentials justify premium valuations. Additionally, price performance can continue particularly in the backdrop of the upcoming MPS with market participants eyeing another rate hike. Our revised TP of PkR249/sh offers 12% upside.

KSE100 - Index	
Current	45,172.99
Previous	45,004.19
Chg.	0.38%

Mkt Cap. (PkRbn/US$bn)	
Current	9,285 / 80.41
Previous	9,245 / 80.07
Chg.	0.43%

Daily Turnover (mn)	
Current	248.11
Previous	235.59
Chg.	5.3%

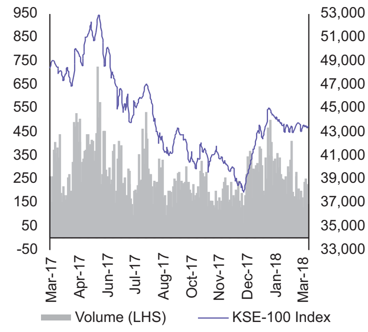
Value Traded (PkRmn/US$mn)	
Current	10,535 / 91.24
Previous	9,437 / 81.72
Chg.	11.6%

News and Views

- Nissan Motor Co. Ltd. is re-entering Pakistan through its local partner, GHNL where the company is to assemble Datsun Cars on the existing assembly lines of the Ghandhara Group. Ghandhara Group has announced to invest up to PkR4.5bn over the next four years and first commercial unit is expected to be rolled out by the end of 1HFY19.

- BAFL has raised PkR7bn Tier-1 capital through perpetual bonds by listing TFCs on PSX which is considered a step towards development of a healthy debt capital market. President of BAFL, Numan Ansari stated that this issue of TFC is going to improve the bank's cash adequacy ratio allowing an additional lending capacity of PkR60bn to the market.

- Power Division's circular debt settlement plan has reportedly hit snags as the Auditor General of Pakistan (AGP) is reluctant to conduct pre-audit of IPPs invoices to make payment announced payments of PkR80bn. The undue delay on part of AGP may lead to shut down of power plants due to financial woes which can lead to load shedding in the upcoming summer season.



Zoya Ahmed
zoya.ahmed@akdsecurities.net
111-253-111 Ext:603

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MCB: Earnings & TP Revision

(PkR/sh)	CY18F	CY19F	TP
New	20.15	23.63	249.1
Old	21.9	23.12	244.5
Change	-8%	2%	2%

Source: AKD Research

CY18F outlook: We believe both the operating environment and MCB's own dynamics will take a turn for the positive from CY18F onwards. In this regard, we expect an uptick in interest rates (+75bps in CY18F) while MCB should be in a much stronger position to reap acquisition benefits of NIB driving our projected 3yr NPAT CAGR of 13.4%. While the impact of the ongoing PIB substitution (~PkR90bn of PIB maturity in Jul'18) is likely to dilute the benefits of an upward adjustment in interest rates, we feel MCB's strategic focus on building its low cost current account base along with the keen urge to grow its advances should counter pressure on NIMs. Additionally, the bank's timely shift towards shorter end maturity profile places it well to benefit from DR upcycle.

Room for upside: NIB's elevated cost structure alongwith credit delinquencies have had their bearing on the merged entity (C/I at 51%, NPL ratio at 9.5% in CY17) and might continue to do so in the short term. That said, we expect rationalization thereon with C/I ratio coming down to 44% by CY20F. With regards to asset quality, the bank's target to recover almost 40-50% or (~PkR11-14bn) of NIB's infected portfolio in the next 3-4yrs seems achievable given MCB's demonstrated execution ability (asset quality amongst the best in the industry pre consolidation), expecting NPL ratio to gradually come down to 6% over the medium term.

Investment Perspective: Having gained 6% since Jan'18, MCB currently trades at a superior valuation set. With peer banks struggling on a number of fronts, we feel: 1) strong capital buffer to take advantage of loan growth opportunities while maintaining dividends at the same time, 2) room for improvement on fee income, 3) aggressive push towards Islamic banking (the only bank to have established a separate subsidiary for its Islamic business) and 4) limited foreign operations are viable justifications in this regard.

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