

PAKISTAN BANKS

MARKET VISTA

REP-019

BAHL: Benefitting from 'Old School' approach

Coverage Initiation

- We initiate coverage on Bank AL-Habib Limited (BAHL) with a 'Buy' stance and a Dec'19TP of Pkr97.6/sh. The stock is currently trading at a CY19F P/B of 1.7x, at a 66% premium to our conventional banking universe. We believe premium valuations are justified considering bank's higher avg. ROE of 21.8% (CY19-21F) vs. our conventional banks' ROE of 16.0% and safe-play features (infection ratio: 1.1%/ coverage ratio: 147.6%).
- Highest interest rate sensitivity amongst our universe of 1.3x, primarily at the back of exceptional loan growth of 40.0% (industry: 20.8%) in CY18 along with potential for balance sheet expansion (117 branches added in the past 2y) perfectly places the bank for strong earnings performance (3y fwd. avg. earning growth: 26.7%).
- We expect higher fund deployment in fixed income securities going forward (IDR to inch-up to 57.8% by CY21 vs. 52.1% in CY18) given attractive risk free returns (3y PIB yield spread: 190bps over KIBOR) and limited good lending opportunities (CY19-21F advances growth: 8.3%, ADR to fall down to 54.3% by CY21 vs. 60.0% in CY18).
- We believe BAHL would fare better than peers in containing its provisioning costs (CY19-21F avg. at 0.25% vs. our universe's 1.0%) considering, i) one of the lowest yield spread amongst our conventional banks (CY18: -0.5% over 3M KIBOR) indicating lending to relatively low risk segments, and ii) coverage standing at 147.6%.

BAHL ideally placed to benefit from interest rate cycle: Highest interest rate sensitivity (interest rate sensitive assets/interest rate sensitive liabilities) amongst our universe of 1.3x, primarily at the back of exceptional loan growth of 40.0% (industry: 20.8%) coupled with branch expansion (117 branches added in the past 2y) succoring deposit growth (3y fwd. avg. deposit growth conservatively assumed at 14.1% vs. industry's 10.3%), perfectly places the bank for strong earnings performance (3y fwd. avg. earning growth: 26.7%). We remain conservative on deposit growth due to potential cannibalization owing to rapid expansion. We expect higher fund deployment in fixed income securities going forward (IDR to inch-up to 57.8% by CY21 vs. 52.1% in CY18) given risk-free attractive returns (3y PIB yield spread: 190bps over KIBOR) and limited good lending opportunities (CY19-21F advances growth: 8.3%, ADR to recede to 54.3% by CY21 vs. 60.0% in CY18). Such diversion would positively impact earnings yield (CY19/20/21F: 10.2/11.0/11.0% vs. 7.1% in CY18) as BAHL earned a negative spread of 50bps over KIBOR on advances in CY18. Resultantly, NIMs of the banks are likely to stand at 4.1/4.4/4.6% in CY19/20/21F vs. 3.6% in CY18 contributing in NII growth of 20.7% (CY19-21F avg.).

A 'Safe bet' in a fragile macro environment: BAHL's cost of provisioning stood at an avg. 1.1% in CY08-11 vs. 1.5% of our banking universe, corroborating the risk conservative strategy of the bank. While risks of default are apparent (GDP slowing down below 4%, interest rate hikes of 450bps in past 15 months, currency depreciation of 25.8%), we believe BAHL would fare better than peers in containing its provisioning costs (CY19-21F avg. at 0.25% vs. our universe's 1.0%). Our prognosis is based on, i) lowest yield spread amongst conventional banks (CY18: -0.5% over 3M KIBOR) indicating lending to lower risk segments, and ii) coverage ratio standing at a strong level of 147.6%. The strong coverage ratio also places the bank in a better position as IFRS-9 gets implemented possibly by CY20. Hence, NIMs net of provisioning is likely to stand at an avg. 4.1% in CY19-21F vs. 3.7% in the past 10y. Together with containment of administrative costs CY19-21F avg. 14.8% vs. 17.3% avg. CY18 as the bank moves ahead from immediate costs of branch network expansion, should contribute to ROE generation.

Investment perspective: BAHL has gained 15.6% in CY19TD, outperforming KSE-100 index by 14.7%, to trade at a CY19F P/B of 1.7x vs. 1.0x of our universe. We believe premium valuations are justified considering higher avg. ROE of 21.8% (CY19-21F) vs. our conventional banks' ROE of 16.0% and safe play features (to note discount of BAHL to our universe in CY08-12, a high risk era, narrowed to 6.4% vs. 12.0% in CY13-17). Hence, with a capital upside of 14.5% and a dividend yield of 4.7%, we have a 'Buy' stance on the stock with a Dec'19TP of Pkr97.6/sh.

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BUY

TARGET PRICE (PKR)	SHARE PRICE (PKR)
97.6	85.3
UPSIDE/DOWNSIDE	DIV. YIELD
14.5%	4.7%

BAHL: Valuations stats

	CY18	CY19F	CY20F
EPS (Pkr)	7.6	9.5	11.9
DY (%)	2.9	4.7	6.4
BVPS	45.0	51.1	60.4
P/B (x)	1.9	1.7	1.4
P/E (x)	11.2	9.0	7.1
ROE (%)	16.8	19.8	21.4
ROA (%)	0.8	0.9	1.0

Source: Company Report, PSX & AKD Research

KATS Code	BAHL
Bloomberg Code	BAHL.PA
Price Pkr	85.3

Market Cap (PkrMn)	93,070.76
Market Cap (US\$m)	669.57
Shares (mn)	1,111.43
Free Float share (mn)	722.43

3M High (Pkr)	87.06
3M Low (Pkr)	68.31

1Yr High (Pkr)	87.06
1Yr Low (Pkr)	66.93

3M Avg Turnover '000	715.88
1 Yr Avg Turnover '000	619.72

3M Avg DT Value (Pkr'000)	56.96
3M Avg DT Value (US\$'000)	0.41

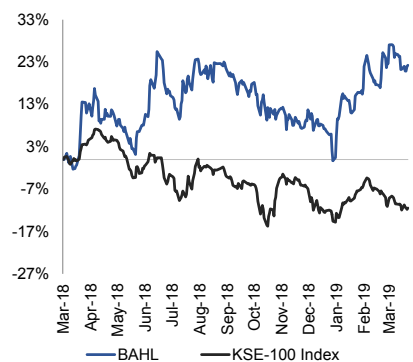
1Yr Avg DT Value (Pkr'000)	48,241.68
1Yr Avg DT Value (US\$'000)	347.06



AKD Securities Limited

BAHL -Annual Financial Databank

BAHL vs. KSE100 Index



Source: PSX & AKD Research

Valuation Multiples

(Year End Dec-31)	CY16A	CY17A	CY18A	CY19F	CY20F
EPS	7.3	7.7	7.6	9.5	11.9
EPS Growth	10.8%	4.4%	-0.6%	25.3%	25.3%
DPS	3.5	3.0	2.5	4.0	5.5
Payout Ratio	48%	39%	33%	42%	46%
BVPS	38.6	41.6	45.0	51.1	60.4
P/E (x)	11.6	11.1	11.2	9.0	7.1
P/BV (x)	2.2	2.0	1.9	1.7	1.4
ROA (Average)	1.1%	0.9%	0.8%	0.9%	1.0%
ROE (Average)	20.1%	19.1%	16.8%	19.8%	21.4%
Dividend Yield	4.1%	3.5%	2.9%	4.7%	6.4%
Market Cap/ Deposits	0.1	0.1	0.1	0.1	0.1
Investment-to-Deposit Ratio	69.4%	68.8%	52.1%	55.7%	56.5%
Loan-to-Deposit Ratio	44.8%	49.1%	60.0%	54.2%	51.6%
Infection Ratio	2.1%	1.5%	1.1%	1.2%	1.3%
Coverage Ratio	136.9%	144.3%	147.6%	146.3%	137.2%
Net Interest Margins	4.1%	3.5%	3.6%	4.1%	4.4%
Cost of provisioning	-0.2%	-0.1%	0.0%	0.1%	0.3%

Income Statement

(PkR mn)	CY16A	CY17A	CY18A	CY19F	CY20F
Net Interest Income	24,687	25,932	30,905	38,547	46,249
Fee Income	2,551	3,182	4,151	5,003	6,721
FX Income	491	914	1,632	1,469	1,028
Dividend Income	555	410	410	588	640
Total Recurring Revenues	28,285	30,438	37,097	45,606	54,638
Capital Gains	723	2,796	(10)	320	393
Other Income	802	896	1,002	1,052	1,104
Total Income	29,809	34,130	38,088	46,977	56,135
Administration Expenses	17,783	19,841	23,264	27,683	32,536
Other Expenses	(530)	502	242	325	398
Profit before provisions	12,557	13,787	14,582	18,969	23,202
Provisions	(638)	(111)	276	696	1,451
Profit before taxes	13,195	13,898	14,306	18,273	21,751
Net Income	8,144	8,499	8,453	10,591	13,268

Balance Sheet

(PkR mn)	CY16A	CY17A	CY18A	CY19F	CY20F
Investments	405,343	476,472	414,981	505,673	581,183
Gross Advances	269,267	347,466	485,945	500,523	540,565
Less: Provisions	7,827	7,632	7,730	8,425	9,876
Advances	261,440	339,833	478,215	492,098	530,689
Total Assets	751,819	919,548	1,019,955	1,147,435	1,273,784
Borrowing	93,717	133,500	119,038	138,585	128,789
Deposits	584,166	692,534	796,852	907,749	1,027,875
Current Deposits	210,377	260,827	287,580	327,602	370,955
Saving Deposits	170,130	195,984	245,657	279,845	316,878
Total Liabilities	708,925	873,270	969,961	1,090,658	1,206,676
Shareholder's Equity Inc. MI	36,221	41,108	46,620	52,830	60,053
Total Equity	42,895	46,278	49,995	56,777	67,107

Source: Company Report & AKD Research

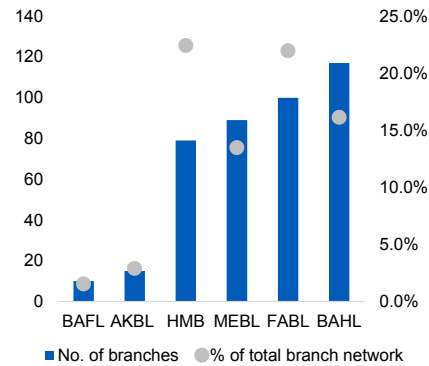
Shareholding Pattern

*As of Dec-2018 Annual Report

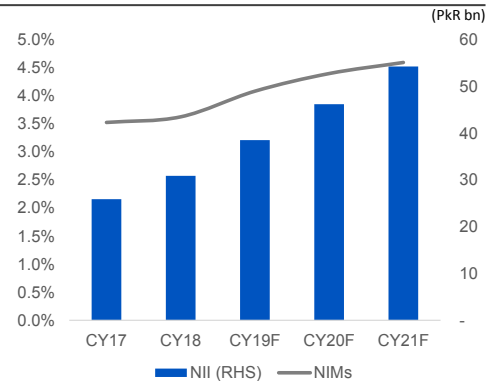
Category	(%)
Individuals	53.62
Investment & Ins Co	11.72
Joint Stock Companies	12.66
Financial Institutions	0.97
Modaraba & Mutual Funds	8.7
Foreign Companies	3.69
Pension Funds	1.26
Others	7.38

Chart bank

BAHL leading branch expansion amongst peers

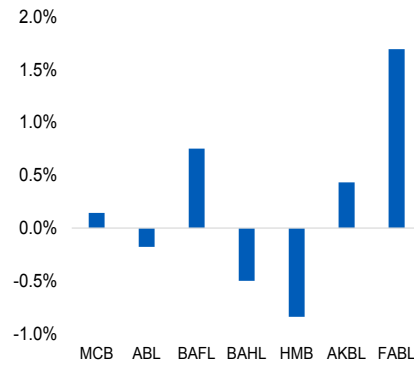


...Along with improving NIMs to support NII growth

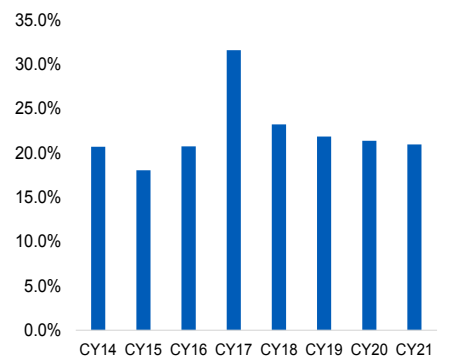


Source: Company Report & AKD Research

Lower yield on advances indicates sound asset quality

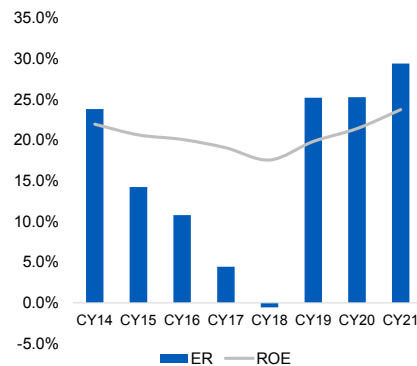


Stable contribution from NFI

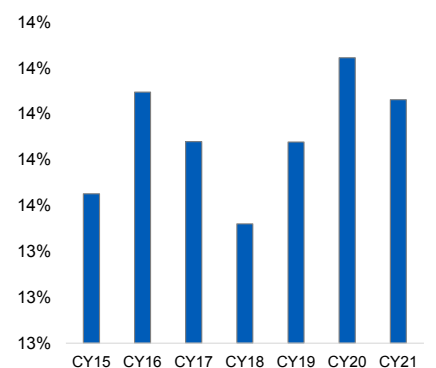


Source: Company Report & AKD Research

.... That should carry earnings growth to >20%



..... which should strengthen CAR



Source: Company Report & AKD Research

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New Rating Definitions

Buy	> 19% expected total return (Rf: 13% + Rp: 6%)
Neutral	> 13% to < 19% expected total return
Sell	< 13% expected total return (Rf: 13%)

Old Rating Definitions (Discontinued)

Buy	> 20% upside potential
Accumulate	> 5% to < 20% upside potential
Neutral	< 5% to > -5% potential
Reduce	< -5% to > -20% downside potential
Sell	< -20% downside potential
Not Rated	No investment opinion or recommendation

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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