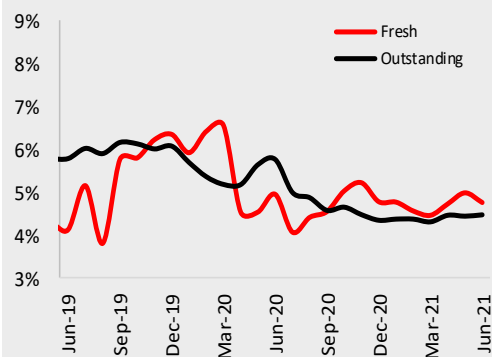


PAKISTAN

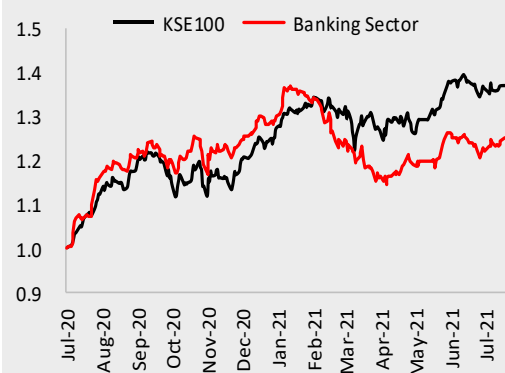


Banking spreads remained under pressure in Jun'21



Source: SBP, Foundation Research, July 2021

Performance of Banking Sector vs. KSE 100



Source: Bloomberg, Foundation Research, July 2021

Analyst

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Foundation Securities (Pvt) Ltd
 Monday, July 26, 2021

Pakistan Banks

Fresh banking spreads declined in Jun'21

Event

As per the data released by the State Bank of Pakistan (SBP), fresh banking spreads for Jun'21 clocked in at 4.77% depicting a decline of 23/19bps MoM/YoY, most since Dec'20. On MoM basis, decrease was mainly driven by significant increase in the deposit rate whereas YoY drop in fresh banking spreads was a result of sharp decline in lending rates. However, weighted average spreads recorded an increase/decrease of 3/129bps MoM/YoY primarily due to higher uptick/decline in lending rates compared to the cost of deposits. Furthermore, deposit base during Jun'21 increased by 10/22% MoM/YoY to close FY21 at Rs19.8tn.

Impact

Fresh spreads took a dip in Jun'21: Fresh banking spreads for Jun'21 clocked in at 4.77% translating into a MoM decline of 23bps, most since Dec'20. This sharp decline in fresh banking spreads was a result of a steep increase in deposit rate 3.43% (↑30bps, MoM) whereas lending rate increased by 8bps MoM to clock in at 8.19% during Jun'21. We suspect that this sharp increase in fresh deposit rate originated by high cost deposits taken by banks to meet the mid-year target which has translated in to 10% MoM increase in the deposit base of scheduled banks. We believe that this is likely to exert pressure on banks' CASA for 2QCY21. On the other hand, weighted average spread of the banking sector increased by 3bps MoM to clock in at 4.48% for Jun'21. This advancement in weighted average spread was a result of higher uptick in lending rates (7.98%, ↑5bps MoM) whereas uptick in deposit cost remained marginal (3.5%, ↑2bps MoM).

Deposit base grew by 22% YoY: During the month of Jun'21 deposit base of scheduled banks posted a growth of 10/22% MoM/YoY to clock in at Rs19.8tn. This increase in deposit base was fueled by impressive growth (10% MoM) registered during Jun'21. Deposit growth is likely to carry on this momentum and post double digit growth in CY21 on the back of uptick in economic activity and the federal government's decision to incentivize lending in the banking system.

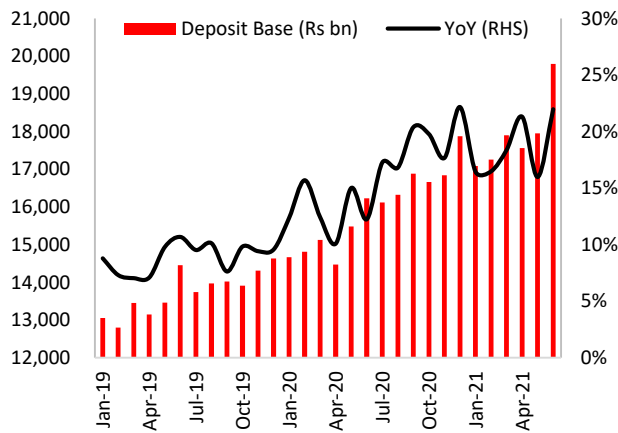
Banks remained inclined towards investments: With the significant increase in the deposit base, investments remained the preferred funds deployment venue for banks. Total investments of the scheduled banks clocked in at Rs13.7tn (↑5/↑29% MoM/YoY) translating into an IDR of 69% with a 3/4ppts decrease/increase MoM/YoY. On the other hand, total advances grew by 2/10% MoM/YoY translating into an ADR of 45% (↓4/5% MoM/YoY). During the same period, credit to private sector also remained upbeat and grew by 3/10% MoM/YoY. We expect credit demand to remain upbeat going forward as a result of uptick in economic activity and government's policies to promote lending. This is likely to fuel up ADRs and have a diluting effect on IDRs.

Yield curve largely remained intact: Since the recovery in economic demand amid higher level of international commodity prices, inflation has been on an upward trajectory. However, these inflationary pressures have been partially offset by concerns of outbreak of delta variant of COVID which has largely kept market expectations, as reflected in largely unchanged yield curve recently, of status quo in interest rates in the short term.

Outlook

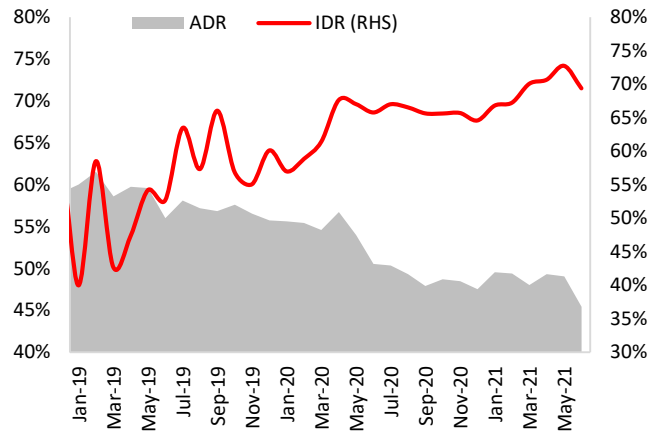
Going forward, we expect banking spreads to remain upbeat on the back of interest rate reversal. In addition to this, we expect deposit growth to remain robust alongwith improving credit demand.

Fig 1: Deposit growth remained upbeat, up 22% YoY



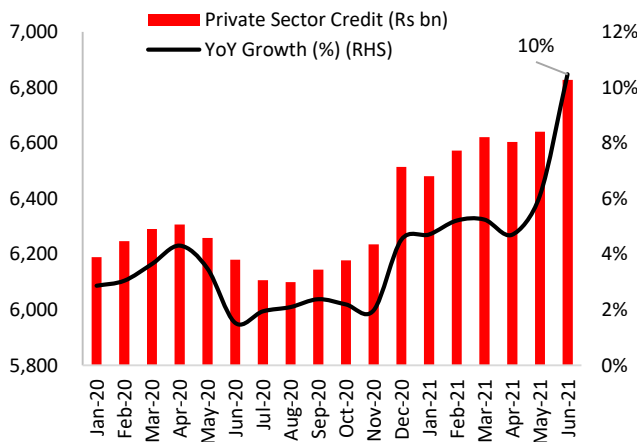
Source: SBP, Foundation Research, July 2021

Fig 2: ...IDRs still remained on the higher side



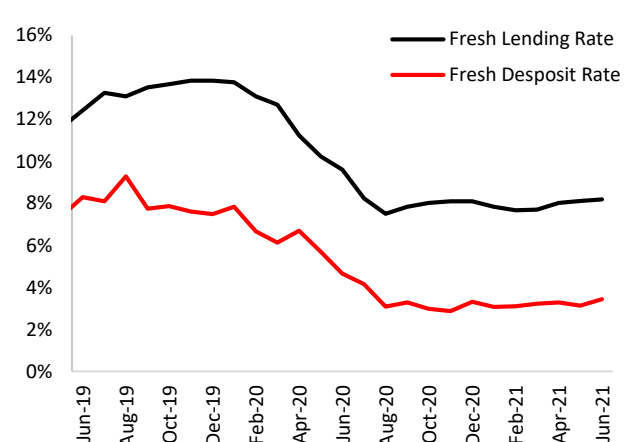
Source: SBP, Foundation Research, July 2021

Fig 3: Private sector credit on road to recovery



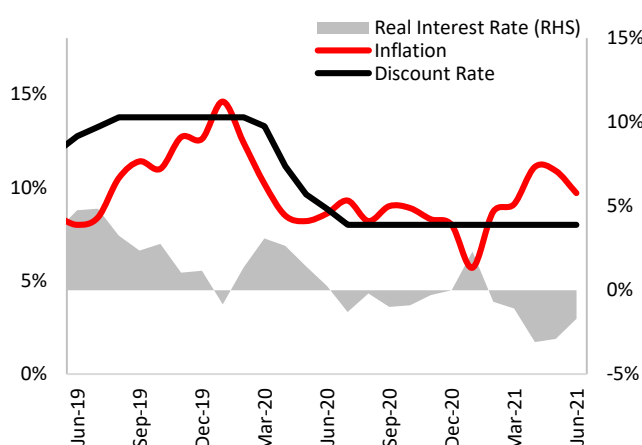
Source: SBP, Foundation Research, July 2021

Fig 4: Fresh banking spreads declined in Jun'21



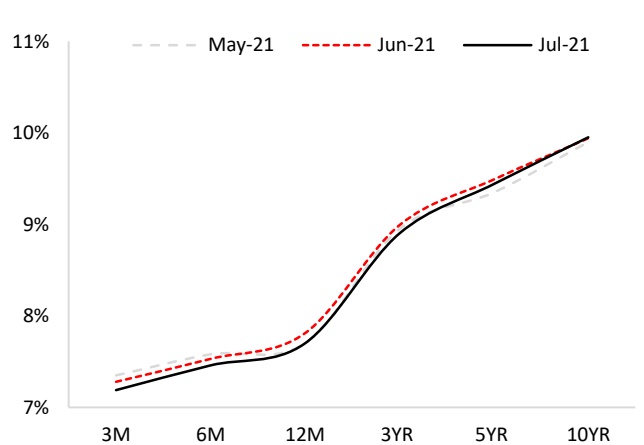
Source: SBP, Foundation Research, July 2021

Fig 5: CPI vs discount rate



Source: SBP, PBS, Foundation Research, July 2021

Fig 6: Yield curve largely remained unchanged...



Source: MUFAP, Foundation Research, July 2021

Abbreviations

NIMs	Net Interest Margins
PR	Policy Rate
NPL	Non-Performing Loans
MoM	Month on Month
YoY	Year on Year
Bps	Basis Points
Bn	Billion
IDR	Investment Deposit Ratio
ADR	Advances Deposit Ratio
M	Month
CY	Calendar year

Important disclosures:

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If	
Expected return >+10%	Outperform.
Expected return from -10% to +10%	Neutral.
Expected return <-10%	Underperform.