

PAKISTAN



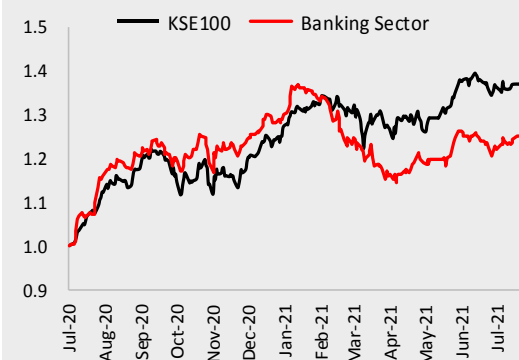
FSL's Banking Universe earnings preview 2QCY21

	2QCY21	2QCY20	YoY	QoQ
UBL	5.39	4.96	9%	-13%
MCB	5.67	5.74	-1%	-4%
MEBL	4.54	4.36	4%	5%
BAFL	1.64	1.62	1%	-14%
AKBL	1.80	2.46	-27%	-18%

Dividend expectation for 2QCY21

	DPS
UBL	4.00
MCB	4.50
MEBL	1.50
BAFL	-
AKBL	-

Performance of Banking Sector vs. KSE 100



Source: Bloomberg, Foundation Research, August 2021

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Pakistan Banks

Lower capital gains to offset incline in NII

Event

▪ FSL banking universe is estimated to witness a drop in profitability ($\downarrow 4/3\%$, YoY/QoQ) in 2QCY21. This decline in profitability is mainly attributed to high base effect on the back of hefty capital gains. However, improvement in Net Interest Income (NII) on the back of increase in banking spreads is expected to restrict the drop in profitability during 2QCY21. UBL, MCB, MEBL, BAFL and AKBL are expected to post EPS of Rs5.39, Rs5.67, Rs4.54, Rs1.64 and Rs1.80 respectively. Aforementioned 2QCY21 results are likely to be accompanied by a DPS of Rs4.00, Rs4.50 and Rs1.50 for UBL, MCB and MEBL.

Impact

▪ **Improvement in NII to partially compensate for lower capital gains:** We estimate FSL banking universe to record a 4/3% YoY/QoQ drop in profitability. Drop in profitability on QoQ basis is primarily driven by lower non-interest income ($\downarrow 8\%$ QoQ) on the back of lower capital gains ($\downarrow 7\%$ QoQ) and uptick in provisional expense ($\uparrow 60\%$ QoQ). However, uptick in net interest income (NII) ($\uparrow 2\%$ QoQ) on the back of improvement in banking spreads is estimated to restrict the decline in profitability. On YoY basis, decline in profitability originates from drop in NII ($\downarrow 13\%$ YoY) which has been partially compensated by the substantial drop in provision expense due to high base effect ($\downarrow 76\%$ YoY). Going forward, we expect improvement in banking spreads and lower provisioning expense (after the deferment of IFRS9 implementation by SBP) to keep the profitability upbeat.

▪ **Deposits remained upbeat $\uparrow 11\%$ QoQ:** Deposit base of banks continued their momentum in 2QCY21 to clock in at Rs19.8tn registering a QoQ growth of 11%. However, pattern of the funds deployment largely remained the same with strong preference towards investments. Total investments of the banking space grew by 9% during the quarter whereas gross advances recorded an increment of 5% during the same period translating into an IDR/ADR of 69/45% vs. 70/48% in the previous quarter.

▪ **Banking Spreads on road to recovery:** Banking fresh/outstanding spreads for the quarter recorded a decent recovery ($\uparrow 23/11$ bps) during the quarter from 1QCY21 average of 4.60/4.35%. Recovery in fresh/outstanding spreads was primarily the result of uptick in lending rates ($\uparrow 37/6$ bps QoQ) while fresh/outstanding deposit rates recorded a minute increase of 15/5bps during the quarter.

▪ **Shift in yield curve:** Yield curve during the quarter witnessed a downward shift as yields declined across all tenors as a result of strong preference from the banking sector. Secondary market yields for 3/6/12-M declined by 14/24/8bps as of June'21 from Mar'21 whereas T-Bills cut-off yields during the period has also come off by 23/22bps in 3/6-M while participation in the 12-M remained lackluster during the quarter.

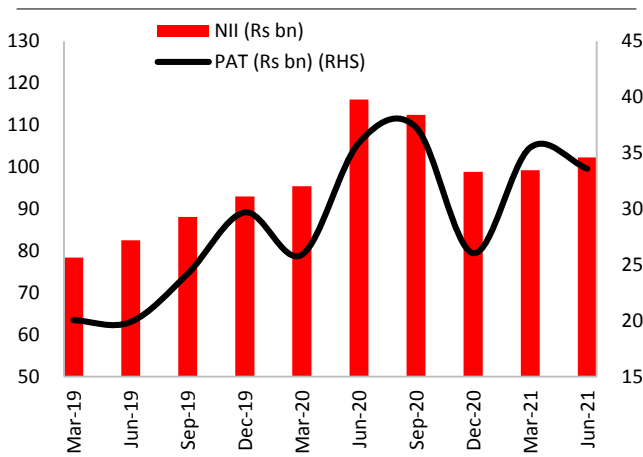
Outlook

▪ Going forward, we expect improvement in banking spreads along with the recovery in NFI to support bottom-line of the banking sector. In addition to this, SBP's decision to defer implementation of IFRS9 amid recovering corporate profitability is expected to keep provisioning expense on the lower side during the ongoing year. Furthermore, taxation measures taken in the in the finance act is estimated to keep profitability of the sector under check. On the balance sheet front, we expect deposit base to continue its momentum with mid-teen deposit growth for CY21 whereas recovery in credit demand may further improve ADR going forward.

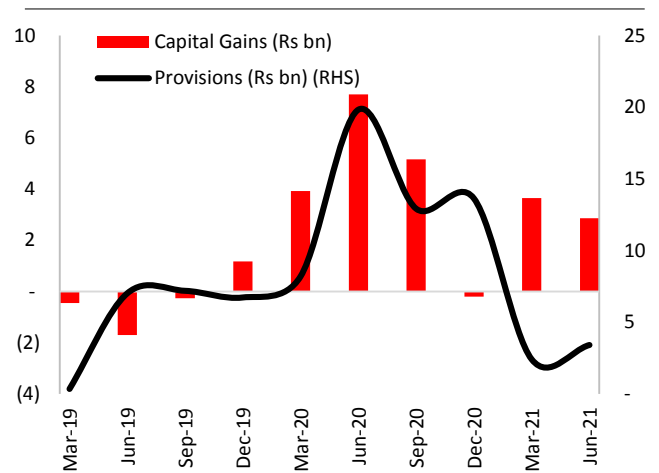
Table 1: FSL Banking Universe 2QCY21 Earnings Preview (Rs mn)

	2QCY21	2QCY20	YoY	1QCY21	QoQ	1HCY21	YoY
Net interest income	101,577	116,097	-13%	99,267	2%	200,844	-5%
Non-interest income	27,886	27,999	0%	30,148	-8%	58,034	13%
Fee income	17,826	12,334	45%	18,096	-1%	35,922	31%
Total Income	129,463	144,096	-10%	129,665	0%	258,878	-1%
Non-interest expense	67,892	63,469	7%	68,039	0%	135,932	4%
Admin expense	66,547	62,201	7%	66,765	0%	133,312	5%
Provisions	3,872	16,139	-76%	2,413	60%	6,285	-74%
PBT	57,606	60,737	-5%	58,865	-2%	116,471	12%
Tax	23,177	24,809	-7%	23,377	-1%	46,553	9%
PAT	34,430	35,928	-4%	35,488	-3%	69,918	13%

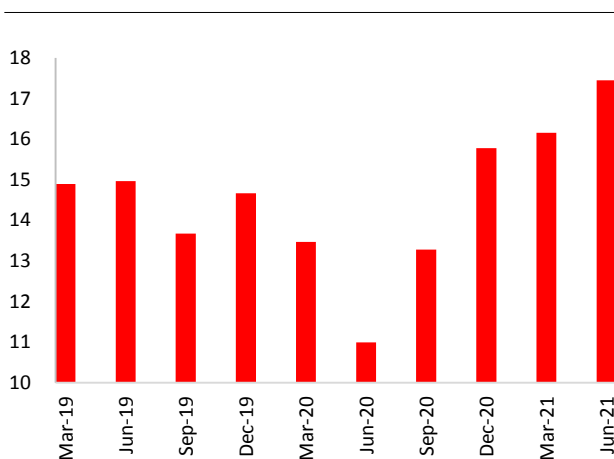
Source: Company Accounts, Foundation Research, August 2021

Fig 1: Profitability of FSL banking universe

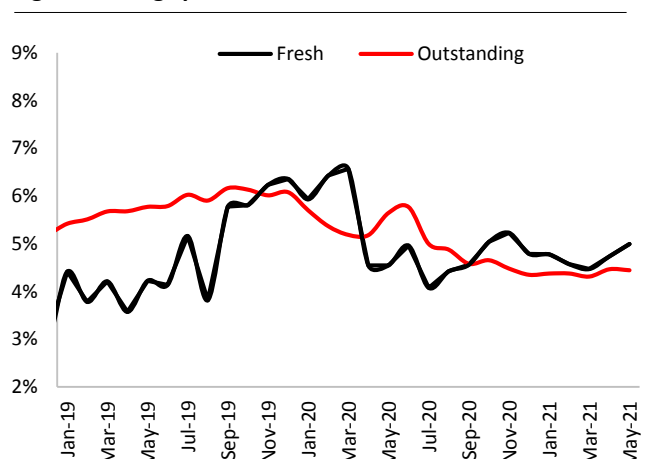
Source: SBP, FSL Research, August 2021

Fig 2: Capital gains and provisioning expense

Source: Company Accounts, FSL Research, August 2021

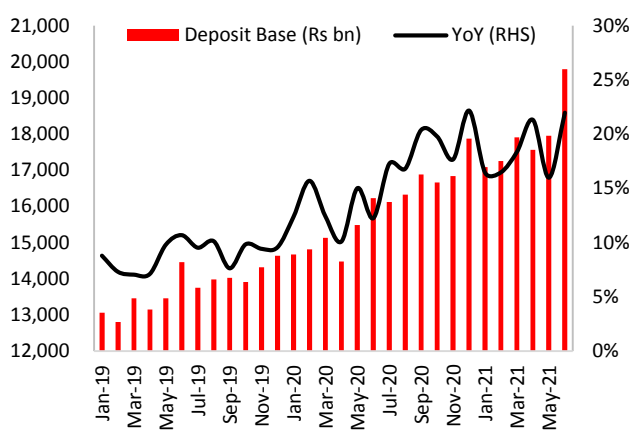
Fig 3: Fee Income showing consistent improvement

Source: MUFAP, FSL Research, August 2021

Fig 4: Banking spreads recovered in 2QCY21

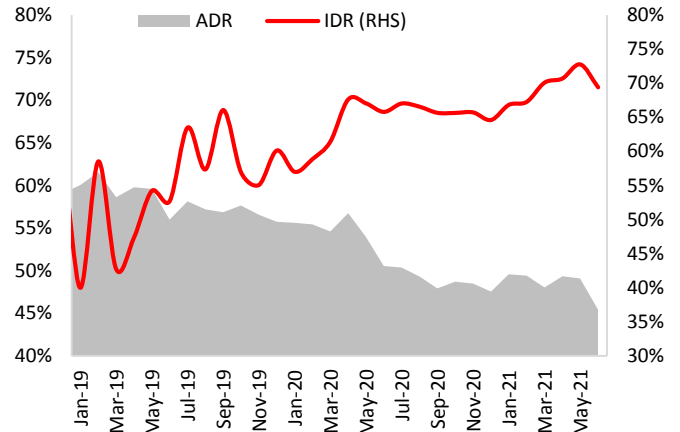
Source: Company Acc, PSX, FSL Research, August 2021

Fig 5: Deposit growth remained robust, ↑22% YoY



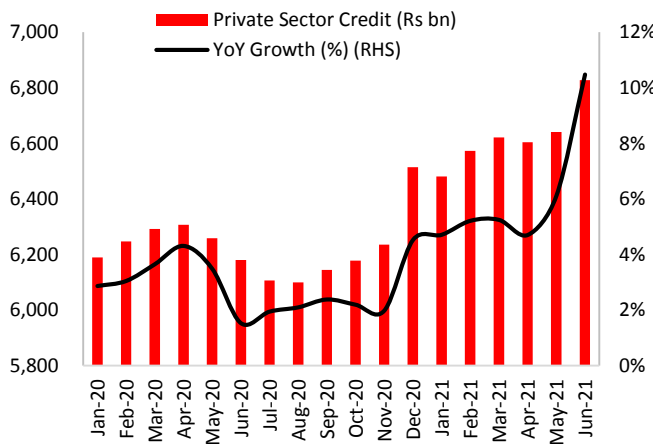
Source: SBP, FSL Research, August 2021

Fig 6: Preference towards investment fueled IDRs



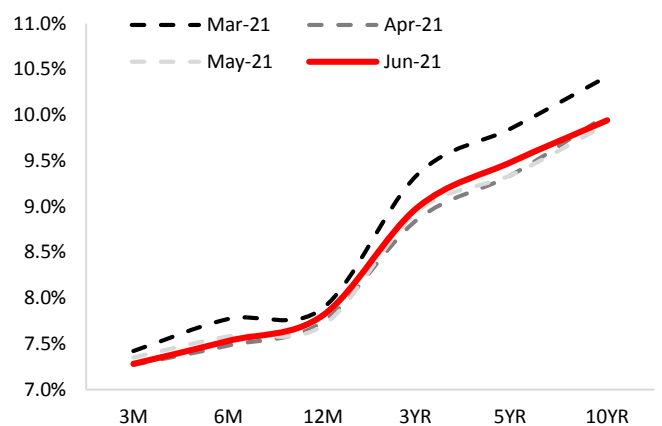
Source: Company Accounts, FSL Research, August 2021

Fig 7: Private sector credit offtake also recovered



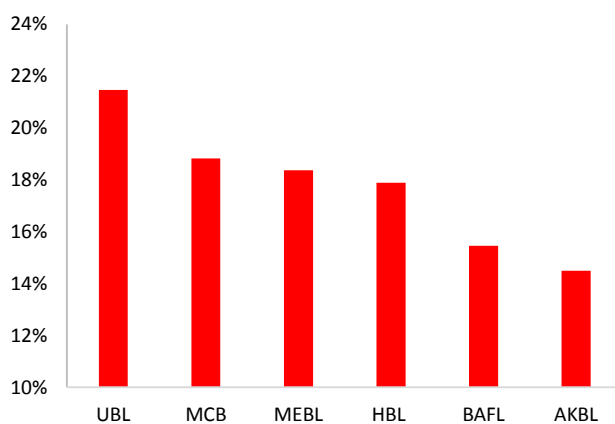
Source: SBP, FSL Research, August 2021

Fig 8: Yields declined across the board



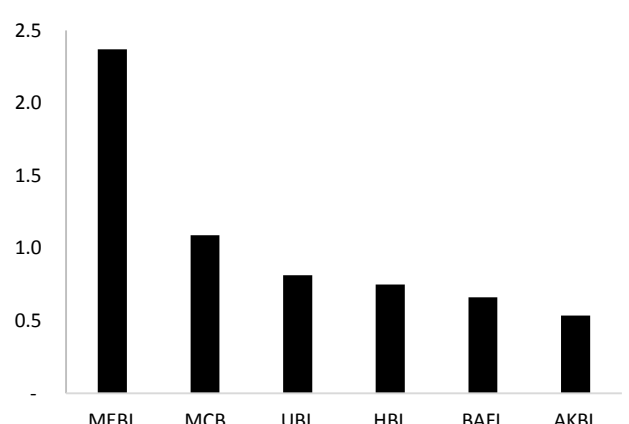
Source: Company Accounts, FSL Research, August 2021

Fig 9: FSL banking universe stands well capitalized



Source: SBP, FSL Research, August 2021

Fig 10: Trading at attractive P/BV



Source: Company Accounts, FSL Research, August 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.