

Foundation Alert

Banks' exposure to Sri Lanka's default

Event

- Sri Lanka has defaulted on its foreign debt because of green back reserve drying out, which has caused Sri Lankan Rupee (LKR) to devalue.
- Amongst the FSL universe, Banks that have exposure include HBL, MCB, and UBL, where UBL only have exposure against its investment book.

Impact

- HBL and MCB have operations in Sri Lanka with 3 and 7 branches respectively.
- UBL has invested from Pakistan in Sri Lanka's Gov't securities.
- Due to the devaluation of Sri Lankan Rupee banks are expected to record translation loss of Rs1.8/Rs1.4/Rs2.7 per share for HBL/MCB/UBL respectively.
- HBL/UBL/MCB investment in Gov't securities of Sri Lanka mounts to Rs8.0/9.0/8.3bn respectively, as of Dec'21.
- Although Banks have not segregated the exposure in their disclosures in terms of currency, if all the Sri Lankan gov't securities are invested in dollar denomination HBL/UBL/MCB would record book value depletion of 5.5/7.4/7.0 per share.

Outlook

- Banks are also awaiting progress on the Sri Lanka gov't front as external financing channels restores and further clarity is visible on economic front in Sri Lanka.

Table 1: Overseas operations- currency translation

	Exposure	BVPS impact
Equity		
HBL	7,459	(1.4)
MCB	6,061	(1.8)
Investment Book		
UBL	9,029	(2.7)

Source: Company Accounts, Foundation Research, Apr'22

Table 2: Impact of default on FSL universe

	Investment in Gov't securities	Book value impact (total US\$ default)
HBL	8,091	(5.5)
UBL	9,029	(7.4)
MCB	8,343	(7.0)

Source: Company Accounts, Foundation Research, Apr'22

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