

Key Points

- Our banking sector coverage universe is expected to post an 8%YoY/7%QoQ decline in earnings during 2QCY21 primarily due to lower NII (with the 625bps reduction in policy rate by the SBP during Mar-Jun 2020) and absence of capital gains. Higher fee & commission income and lower provisions are expected to restrict the shrinkage in bottom-line.
- Banking sector deposits as on June 30, 2021 have reported a 14-year high growth in 2Q of 22%YoY while advances have also managed to accelerate growth to 10%YoY, with the excess liquidity being parked in investments, which have grown by 29%YoY.
- We believe that the sector fundamentals are intact and the continued underperformance of the sector provides an opportunity for accumulation of big banks that offer attractive valuations and higher payouts. UBL, HBL, MCB and BAFL are our preferred picks at current levels.

Combined earnings to decline by 8%YoY in 2QCY21

We present 2QCY21 earnings estimates for our banking sector universe, wherein we expect the combined earnings of our coverage universe to report a dip of 8%YoY/7%QoQ. The YoY decline in earnings may be attributable to lower NII that is expected to shrink by 8%YoY (with the 625bps reduction in policy rate by the SBP during Mar-Jun 2020) along with absence of capital huge gains this quarter. A healthy recovery in fee & commission income of the sector coupled with lower provisions charge are expected to restrict the bottom-line shrinkage. During 1HCY21, the combined earnings are expected to register a modest growth of 11%YoY despite an estimated 2% decline in NII. The growth is expected to be fuelled by higher non-interest income despite lower estimated capital gains and significant reduction in provisions charge.

Healthy growth in deposits leading to higher investments

Deposits during the quarter reported an increase of 22%YoY (highest 2Q YoY growth after 24.2% in Jun'07) to PKR19.8tn whereas advances also managed to accelerate growth to 10%YoY to PKR9tn. The higher liquidity however continued to be parked in investments that registered a growth of 28.7%YoY to PKR13.7tn. At the end of 2QCY21, ADR/IDR of the banking sector stood at 45.4%/69.4% compared to 47.5%/64.6% of Dec'20.

Next Bank Universe

PKRmn	2QCY21E	2QCY20	YoY	1QCY21	QoQ	1HCY21E	1HCY20	YoY
Interest/Profit Earned	228,588	260,906	-12%	217,959	5%	446,547	531,899	-16%
Interest/Profit Expensed	110,154	131,910	-16%	106,328	4%	216,482	296,168	-27%
Interest/Profit Net	118,434	128,996	-8%	111,631	6%	230,065	235,731	-2%
Fee, Commission, etc.	20,235	13,996	45%	20,314	0%	40,549	30,789	32%
Dividend Income	1,129	891	27%	1,286	-12%	2,415	1,678	44%
Income from FX	4,050	4,058	0%	4,230	-4%	8,280	6,936	19%
Capital Gains/(Losses)	59	10,574	-99%	4,533	-99%	4,592	14,945	-69%
Others	2,182	2,676	-18%	2,618	-17%	4,800	3,179	51%
Non-Interest Income	27,656	32,195	-14%	32,981	-16%	60,637	57,525	5%
Total Income	146,090	161,191	-9%	144,612	1%	290,702	293,256	-1%
Operating Expenses	77,213	69,433	11%	75,531	2%	152,745	142,136	7%
Provisions & Write-offs	7,358	23,750	-69%	3,208	129%	10,566	33,051	-68%
Others	1,401	1,560	-10%	1,476	-5%	2,877	3,692	-22%
Profit Before Tax	60,117	66,447	-10%	64,397	-7%	124,514	114,378	9%
Tax	23,609	27,214	-13%	25,196	-6%	48,805	46,834	4%
Profit After Tax	36,509	39,217	-7%	39,200	-7%	75,709	67,533	12%
Profit for Equity holders	36,250	39,375	-8%	38,952	-7%	75,202	67,660	11%

* Consolidated accounts for HBL, UBL, MCB

Source: Company Accounts, Next Research

Outlook

We maintain our overweight stance on the sector while it has been a major underperforming sector. We believe that sector fundamentals are intact considering double-digit growth in deposits, resumption in advances growth, expected hike in interest rates, and slowdown in provisions with improved coverage ratios after the handsome amounts of general provisions booked by the sector during 2020. While we have buy recommendations on all of our coverage banks, we prefer big banks that offer attractive valuations and higher payouts including HBL, UBL, MCB and BAFL.

Pakistan Equities Commercial Banks

Key Data

Mkt. Cap. (USDmn)	2,161
Mkt. Cap. (PKRbn)	348.4
Index Weightage (KSE-100)	17.2%
Number of Listed Companies	19

Source: PSX, Next Research

EPS estimates

	2Q21E	YoY	QoQ	1H21E	YoY
BAFL	1.54	-1%	-21%	3.50	11%
BAHL	3.73	-5%	-10%	7.87	21%
BOP	0.55	-33%	-21%	1.24	-10%
HBL*	5.88	-22%	4%	11.57	12%
MCB*	5.97	4%	1%	11.89	5%
MEBL	3.88	20%	-10%	8.19	51%
UBL*	5.49	11%	-12%	11.70	31%

* Consolidated accounts for HBL, UBL, MCB

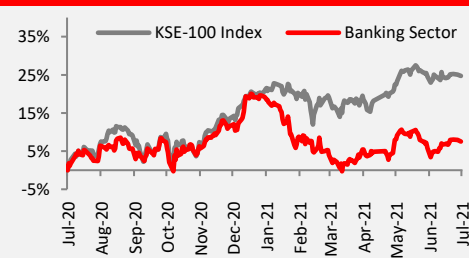
Source: Company Accounts, Next Research

DPS estimates

	2QCY21E	1HCY21E
BAFL	2.00	2.00
BAHL	-	-
BOP	-	-
HBL	1.50	3.25
MCB	5.00	9.50
MEBL	1.50	3.00
UBL	4.00	8.00

Source: Company Accounts, Next Research

1 Year Relative Performance



Source: PSX, Next Research

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Rating	Sector's proposed weight in the portfolio
Over Weight	> Weight in KSE 100 index
Market Weight	= Weight in KSE 100 Index
Under Weight	< Weight in KSE 100 Index

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Rating	Expected Total Return
Buy	$R \geq 15\%$
Neutral	$0\% \geq R < 15\%$
Sell	$R < 0\%$

Where;

$R = \text{Expected Dividend Yield} + \text{Expected Capital Gain}$

R' is before tax

Investment horizon is between six months to twelve months

Ratings are updated regularly based on the latest developments in the economy/sector/company, changes in stock prices, and changes in analyst's assumptions.

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