

March 02, 2009

Pakistan Market**HBL: Company Update/Downgraded to 'Sell'****MORNING BRIEFING**

KSE100 Index Closing 5727.46 ↑ (+77.97)

Habib Bank Limited (HBL) recently announced its full year 2008 results with earnings of Rs13.2/share and a dividend and bonus payout of Rs5.5 & 20% respectively. While earnings depicted a growth of 24%YoY led by strong showing of net interest & non interest income, recognition of Rs2.0bn impairment loss and rising Non Performing Loans (NPL) ratio remained major highlights of the financial accounts.

In today's report, we discuss HBL's financial performance in 2008 along with our updated outlook on the stock after incorporating the detailed financial results.

17% NII growth drives earnings up 24%

HBL's earnings rose 24% to Rs10.0bn (EPS Rs13.2) mainly driven by 17% rise in net interest income (NII) to Rs35.6bn amid rising spreads and net interest margins (NIM). The bank's NIM rose by 40bpsYoY on account of higher yields on earning assets as interest spreads widened by 33bps during the year. Moreover, Advances to Deposit Ratio increased by 500bps amid slowing deposit growth, which contributed to the growth in NII. Going forward given lower credit offtake & crowding out of deposits by the government, both NIM and spreads are likely to contract considerably, which would in turn affect NII growth.

Non interest income up 21%, impairment Rs2.0bn

In addition to strong NII growth, HBL's earnings were well supported by 21% rise in non interest income on account of double digit growth in both fee income & income from forex transactions. Exchange rate volatility helped 57% growth in income from forex dealings to Rs2.4bn, while increasing trade activity and other business transactions helped HBL increase its fee & commission income by 21% to Rs4.2bn.

Despite strong growth in NII and non interest income, earnings growth was largely diluted by the recognition of Rs2.0bn (Rs1.7/share) impairment loss on investment in available for sale securities (AFS), associates and subsidiaries. HBL's decision to recognize the entire loss in

2008 despite option to defer the recognition to 2009 is a bold move that helps to objectively present the financial performance of 2008.

NPL provisions fall 17% but NPL ratio rose to 8.3%

Provisions for non performing loans expectedly declined by 17% to Rs6.7bn due to absence of huge Forced Sale Value charge recognized in last quarter of 2007. The major point of concern for HBL however, has been the sharp rise (47%) in NPLs to Rs36.0bn. Resultantly NPL ratio has gone up by a massive 150bps to 8.3% and clearly signals substantially high provisions in 2009. Given considerable decline in industrial production and HBL's substantial exposures to textile sector (21% in 2008), we expect provisions for NPLs to increase to Rs7.7bn in 2009.

Outlook: "Downgraded to sell"

HBL's share price had rallied in Feb 2009 in anticipation of strong results and good payout, however we believe risk of rising NPLs and depressed NIMs remain key future challenges. Hence, we have downgraded our stance on the scrip from 'Hold' to 'Sell'. The bank trades at a 2009E PE and PBV of 8.5x and 1.1x, respectively, while it offers a 2009E ROE of 13.5%.

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Habib Bank Limited**Market Price:**

Rs102.13

Market Cap:

Rs77.5bn (US\$969.9mn)

1-yrs Avg. Daily Volume:

0.6mn shares, Rs116.3mn (US\$1.5mn)

1-year High/Low:

Rs319.00/51.17

Kats Code:

HBL

Bloomberg Code:

HBL PA

Reuters Code:

HBL.KA

Also in focus**Shaukat Tarin to give details of IMF review today**

According to newspaper reports, Finance Advisor Mr. Shaukat Tarin is expected to address the media today to make public, details of the recent review by IMF on the Pakistan's economy held in Dubai. Moreover, he is expected to give clarity on reported concerns emerging in the IMF camp over political turmoil in Pakistan. According to reports, IMF fears political turmoil will make it difficult for the government to achieve the agreed economic targets.

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