

January 14, 2010  
Pakistan Market

MORNING BRIEFING

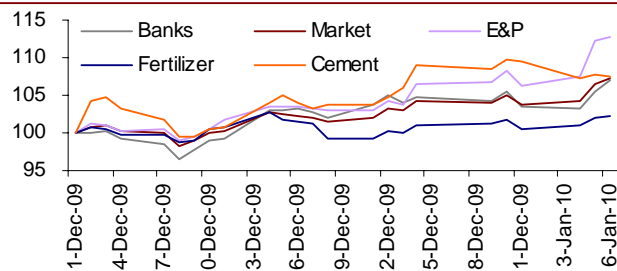


## Banking sector: Management meetings update

KSE100 Index: Closing 9784.85 ↑ (+6.49)

Banking sector with a market capitalization of Rs707bn (25% weight in KSE) has largely underperformed in the recent rally mainly due to concerns about provisions and outlook for credit growth. We find the sector far too important to ignore, given its weight in the KSE and hence we conducted a series of meetings with management of major banks. The purpose behind these was to get their views on various issues facing the sector and their outlook for 2010. A general consensus that emerged from the discussions was that the provisions are on their way down, credit growth is likely to be in the range of 7-10% in 2010, while anticipated foreign inflows should drive deposit growth to double digits in the current year.

Graph: Banks performance v/s market and key sectors



Source: KSE

### Provisions likely to fall sharply in 2010

In line with analyst expectations, the managements of major banks expect provisions to drop sharply in 2010 as NPL accretion slows and asset prices start to recover. This would serve as a major catalyst for the earnings growth in 2010, as nearly 32% of the net interest income was absorbed by provisions in 9M2009. Moreover, adequate coverage of 70% (particularly after taking note of the FSV benefit) also supports this assertion, which is likely to be validated by the annual results for 2009.

### Foreign inflows to drive deposit growth

Banks are gearing up in anticipation foreign inflows coming from KLB and FODP and expect deposit growth to be in double digits in 2010, broadly in line with the GoP's money supply expectations. This would help bring deposit rates down and would partially mitigate the impact on NIMs from an anticipated decline in KIBOR.

Managements are of the opinion that contraction in NIMs are likely to be limited to 20-40bps in 2010, however, a double digit asset growth and a significantly lower quantum of provisions would mean earnings will still grow by 15-20% in 2010. The pick up in credit growth would still be slow (7-10%) and would be largely concentrated towards the corporate and commodity sector, with some minor improvement in consumer lending, particularly, in the second half of 2010.

### Outlook: The worst seems to be over

Post the recent round of discussions with major banks, we believe, the worst is over and banks are likely to gradually catch up in terms of market performance in the coming months. The upcoming result season would serve as a starting point in this regard. We currently have a 'Market-Weight' stance on the sector with NBP and BAFL our preferred picks at current levels.

Table: Valuation of key banks (2010F)

	PE (x)	PBV (x)
Allied Bank	6.4	1.5
Bank Al-Falah	6.9	0.8
Habib Bank	8.9	1.5
MCB Bank	8.1	1.8
National Bank	6.2	0.7
United Bank	7.5	1.2

Source: JS Research

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### Also in focus

#### Thal Limited: Analyst Briefing Update

Thal Limited conducted its first ever analyst briefing yesterday. The management in its presentation, particularly discussed the updates on its retailing arm namely Makro highlighting the land dispute regarding one of its outlets. Makro-Habib has been asked by the Supreme Court to shut down its operations and restore the 4.9 acres of land to its original condition. As per the management, shutting down of the store would lead to an impairment loss of Rs550mn, of which Rs223.48mn would be recorded on Thal's books (Thal Limited has a 55% stake in the company). This in turn would lead to a one time loss of around Rs4.3 per share. Additionally, the closing of the store would impact the future revenue stream as the outlet contributes a little over 20% to the total revenues generated by the Makro chain. To recall, Thal Limited reported consolidated earnings of Rs902mn (EPS: Rs18.92 per share) in FY09, and Rs152mn (EPS: Rs4.84 per share) in 1QFY10.

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