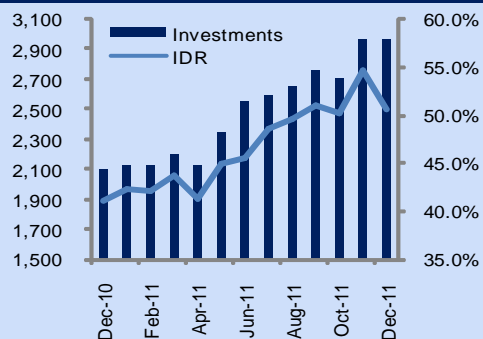


Banking Sector

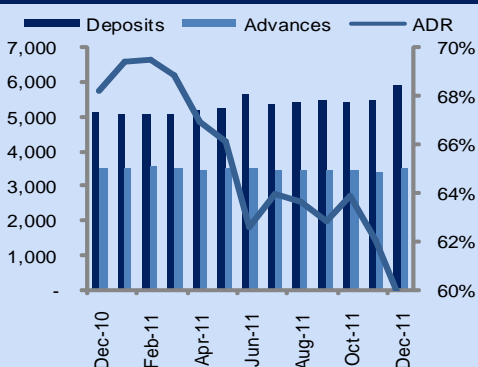
Advances remain stagnant, while investments increase unabated

Investments to Deposit ratio



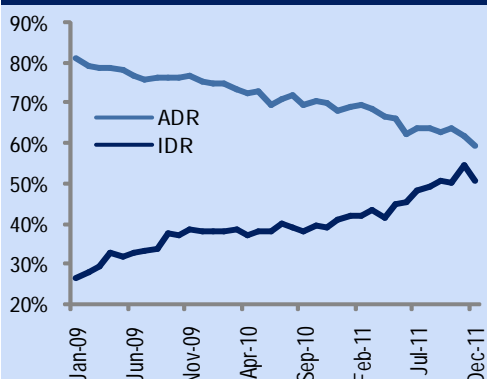
Source: SBP

Advance to Deposit ratio



Source: SBP

Converging ADR and IDR



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CY11 turned out to be a phenomenal year for the banks as their profitability jumped by 55% YoY till Sept-11 resulting in ROEs to improve from 9.9% in Sept-10 to 14.1% by Sept-11. This situation arose as high spreads led to high NIMs while provisioning charge contracted by 11% YoY. The banking deposits grew by 14.6% YoY in CY11 while advances remained stagnant during the period. Going forward in CY12, the sector is likely to witness contraction in NIMs as the interest rate was slashed by 150bps to 12% effective from Oct-11. We believe banks will continue to retain their high exposure in government backed securities for now. However, if SBP further slashes the discount rate (our stance on upcoming MPS is a hold) banks would be compelled to increase dwindling their Advance to Deposit Ratio (ADR), which are at its lowest since CY02. In CY12, banking sector is likely to post flattened earnings growth.

	Dec-11	Dec-10	YoY	Nov-11	MoM
Deposits	5,874	5,124	14.6%	5,416	8.5%
Advances	3,493	3,494	0.0%	3,357	4.0%
Investments	2,970	2,102	41.3%	2,962	0.3%
ADR	59.5%	68.2%		63.9%	
IDR	50.6%	41.0%		50.3%	

Source: SBP

Deposit growth continues unabated

The banking sector deposit growth, as of Dec-11, has slowed down to 14.6% compared to 18.5% in the corresponding period last year. In CY11, broad money (M2) appreciated by 13.7%, the slowest pace in the last two years. By the end of CY11 deposits have reached PKR 5,874bn compared to PKR 5,124bn in CY10. On MoM basis, deposits augmented by 8.5% in Dec-11 which during July-Nov 2011 period averaged PKR 5,386bn. This situation is reflective of the historical trend where deposits witnessed higher growth pattern in June and December.

Banking Sector advances remain stagnant in CY11

The banks' focus during CY11 was primarily towards investments which have subsequently resulted in advances remaining stagnant on YoY basis at PKR 3,492bn by end of Dec-11. This situation has led to banking sector Gross ADRs to drop from 68.2% last year to 59.5%, which is the lowest in the last decade. The banks' hesitancy towards advances primarily emanated from rising Non-Performing Loans (NPLs) which by Sep-11 has jumped by 11.9% YoY to PKR 613bn. By Sept-11, the gross infection ratio has clocked in at 16.7% compared to 14.7% in CY10. Even though the banks tried to restrain their falling loan default ratio, high interest rates and deteriorating economic indicators along with growing energy crisis and circular debt countered any positive outcome.

Investments jumps by 39% YoY with IDR reaching 51%

The banks' continuous focus remained tilted towards investment side, which on monthly average basis has registered a rise of 39% YoY to close the year at PKR 2,970bn. In CY11, Investment to Deposit Ratio (IDR) has jumped to 51% from 41% in CY10. The rise in banks' exposure towards investment side has amplified since CY09 as both interest rates and private sector NPLs have increased. The

banks have increased their exposure in government securities which by Nov-11 had grown by 74%. In Nov-11, government converted TFCs and loans related to circular debt worth of PKR 391bn into T-bills and PIBs worth approximately PKR 195bn. Consequently, T-bills, whose share in investment is around 71% (CY10: 60.2%) have amplified by 66% while investment in PIBs has increased 2.2times to PKR 472bn by Nov-11.