

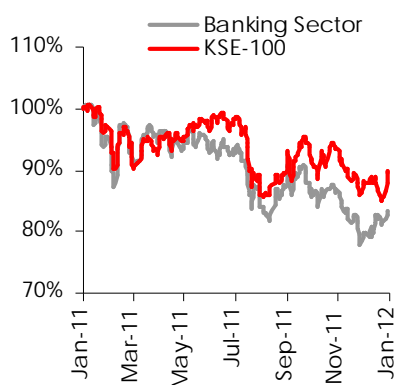
**Pakistan Research**

Banking Sec. Mkt. Cap. Rs598.59bn  
 Top Pick (s): UBL,FABL  
 Sector Outlook: Neutral  
 Banking Univ. P/E (2012F) 4.84x  
 Banking Univ. Div. Yield (2012F): 9.60%  
 Banking Univ. Ear. Growth (2012F): 1.40%

## Banking Sector - A comparison of capital strength

### Highlights

- NBP pulling the top tier banks down
- Big 5 by name, very big 5 by capital strength
- Banks short on MCR tell a different story



In today's value seeker we present a comparison on the asset infection of the top tier banks against our sample of banks that have been unable to meet the MCR prescribed by SBP. Coupled with an analysis about the strength of their capital if they fully provide for their NPLs and contingencies

### NBP pulling the top tier banks down

At the time when the advances of the whole banking sector are stagnant, a stupendous rise in asset infection points not only towards lack of risk management measures taken by the sector, but also towards the dilemma faced by different economic sectors due to major problems such as deteriorating law and order situation and the ever escalating energy crisis. Cumulative NPLs of the big 5 banks have risen by worrying 20% during 9MCY11, the majority of the stress in the NPLs head is provided by NBP. The bank's NPLs during the period under consideration ballooned up by astounding 36% (above by massive 24pps to its closest peer, UBL whose NPLs grew by mere 12% during the same period). This highlights the absence of proactive risk management system at NBP. In addition to that, Bank's provisioning however, failed to keep up with the increase witnessed in its infection and as a result net NPLs of the bank have risen by alarming 36% during 9MCY11. This has pushed the net NPLs of the big 5 upward by 47%.

#### TOP TIER BANKS' CAPITAL STRESS TEST

(Rs mn)	NBP	MCB	ABL	UBL	HBL	Big 5
Capital	104,819	77,501	35,202	74,362	96,765	388,649
Gross Advances	579,672	263,564	249,297	366,433	492,967	1,951,934
Gross NPLs	118,226	26,463	20,549	54,541	59,064	278,843
Provision	66,432	22,001	16,688	40,690	47,217	193,029
Net NPLs	51,794	4,462	3,861	13,851	11,847	85,815
Contingencies	8,467	862	4,620	22,202	84,114	120,265
Capital Post Stress test	44,558	72,178	26,720	38,310	804	
Gross infection	20%	10%	8%	15%	12%	14%
Net Infection	10%	2%	2%	4%	3%	5%

Source: Company Reports, InvestCap Research

### Big 5 by name, very big 5 by capital strength

However, despite having such a high rate infection at 14% during 9MCY11 as compared to 12% during CY10, the big 5 banks have enough reserve backing that even if they fully provide not only for their NPLs but for their contingencies (claims against banks not classified as debt). This somewhat lessens the mounting infection risk that is being faced by the big 5 and conversely, highlights their strength and dominance in the banking sector. However, it must be kept in consideration that apart from NBP, all the top tier have had nominal growth in NPLs' (between 10-12%), but their cumulative advances have shrunk by 3% during 9MCY11. However, NBP is the only one of the big 5 that has bolstered its advances by 8% during 9MCY11.

### Banks short on MCR tell a different story

Being in the lower tier, the banks that are yet to meet the MCR requirement, have to run an extra mile to conduct their business. This suggests that these banks are more than willing to pay higher rates to attract deposits. Similarly, they are more likely to invest in riskier assets at lower cost mainly to attract business. This would suggest that risk management system has to work over time to make sure that the asset quality remains intact. However, this is not the case as one fourth of these banks' cumulative assets are infected. On the hind side, being small size banks, they do not enjoy the same amount of reserve cushion against any shock if these NPLs are fully provided for. We have given a table below that depicts the dire capital position of the banks if they are to fully provide for NPLs and contingencies.

#### LOWER TIER BANKS' CAPITAL STRESS TEST

(Rs mn)	KASB	SILK	JS Bank	SUMMIT	Total
Capital	2,339	5,031	6,062	5,629	19,060
Gross Advances	32,968	52,777	13,069	67,151	165,965
Gross NPLs	11,768	10,565	3,113	11,635	37,081
Provision	6,079	7,316	508	11,033	24,935
Net NPLs	5,688	3,249	2,605	603	12,146
Contingencies	-	352	66	2,587	3,005
Capital Post Stress test	(3,350)	1,429	3,390	2,439	
Gross infection	36%	20%	24%	17%	22%
Net Infection	21%	7%	21%	1%	9%

Source: Company Reports, InvestCap Research

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