

31 August 2016

Abdul Ghani Fatani

abdul.ghani@imsecurities.com.pk

+92-21-37131600 Ext: 305

Inter Market Pulse

Pakistan Banks

NBP: Turnaround reflecting in results; upgrade to Buy

- We upgrade NBP from Neutral to Buy with a revised Dec'17 TP of PkR83/sh (Dec'16 TP PkR66/sh earlier), which offers a potential total return of 33%. EPS estimates for CY16/17F have been revised up by 6%/8% to PkR9.71/10.24 on the back of turnaround underway since CY15, which is likely to unlock long awaited earnings potential.
- Since its CY16TD low, the stock has outperformed the IMS Bank Universe by a staggering 26%. We believe this is a function of growing investor confidence on (i) consistent improvement in asset quality and cost efficiencies, and (ii) tremendous potential of non-interest income. The stock trades at CY17F P/B of 0.86x, where narrowing of valuation discount (larger private banks P/B: 1.5x) can unlock upside.
- 2QCY16 earnings of PkR2.84/sh surpassed consensus expectations with support from (i) 10%YoY/31%QoQ rise in NII, (ii) lower loan provisions, (iii) impressive 34%YoY rise in fee income, and (iv) contained 9%YoY increase in admin cost (C/I: 51%). Surprise element in 2H may materialize from unrealized capital gains of PkR45.6bn (on equities: PkR27.8bn)

NBP upgraded to Buy: We upgrade National Bank of Pakistan (NBP) from Neutral to Buy with revised Dec'17 TP of PkR83/sh (from previous Dec'16 TP of PkR66/sh), which offers a striking total return of 33%. EPS estimates for CY16/17F have been revised up by 6%/8% to PkR9.71/10.24, supported by visible result turnaround since CY15, which is likely to extend in the medium term, in our view.

Diminishing asset quality concerns: Among the positives, NPL ratio has come off by 2.3ppt to 17.8%, backed by recent prudent lending approach (3%YoY loan growth lags behind industry growth of 12%YoY), with coverage of 88% likely to keep credit costs in check going forward. Support can emanate from completion of cleanup exercise on the international front; pre-provision profits from international operations doubled in 1HCY16.

Unique fee income characteristics could lead to outperformance: We believe (i) 50% increase in ATM network in CY16F, (ii) introduction of bancassurance in over 600 branches, coupled with debit cards, and (iii) increasing footprint of tax and GoP fee collection beyond the designated 600 branches to over 100,000 agents and ATMs can support robust growth in this area. Other than this, unrealized capital gains backlog of PkR45.6bn (pre-tax; 2.2x CY16F NPAT) has the potential to surprise in 2HCY16.

Limited cost growth: Cost efficiencies are coming into play, but C/I of 51% still lags behind peers. We believe (i) possible net retirement of 5000 employees over next few years, (ii) planned measures like changes in medical allowance policies, and (iii) centralization of processes can support the cause.

Stock price is up and running: Since its CY16TD low, the stock has muscled through with a run-up of 44%. We believe the market has been quick to appreciate the recent turnaround in the bank, which has long been penalized for having (i) inherent asset quality issues, and (ii) poor cost administration. The stock currently trades at a CY17F P/B of 0.86x, where narrowing valuation discount is likely to unlock further upside. Payout remains a stand-out element, with a 10% dividend yield looking more attractive than traditional IPP plays; sustainability will prevail considering CAR is at over 18%. Any shift from an annual to quarterly dividend policy can further catalyze volumes and stock performance.

2QCY16 Earnings: Turnaround more visible: During 2QCY16, NBP posted consolidated NPAT of PkR6.05bn (EPS: PkR2.84), which comfortably surpassed street consensus on the back of (i) 10%YoY/31%QoQ rise in NII, mainly led by 54%YoY increase in investments, (ii) lower loan provisions (PkR879mn vs. PkR3.7bn in 2QCY15), (iii) 34%YoY rise in fee income, and (iv) cost efficiencies clearly coming into play with contained rise in admin costs (up 9%YoY in 2Q). On the balance sheet front, loan growth recovered (up 3%YoY) after posting consecutive declines in the last 4 quarters; but it still remains much lower than peers.

National Bank of Pakistan

Price (PkR/sh)	73.7
TP (PkR/sh)	83.0
Stance	Buy
Upside	12.7%
Fwd D/Y*	20.7%
Total Return	33.4%
Bloomberg / Reuters	NBP PA / NBPK.KA
Mkt Cap (US\$m)	1,496.4
52wk Hi-Low (PkR/sh)	73.65-51.15
3m Avg. Daily Vol ('000 shrs)	1,733
3m Avg. Traded Val (US\$m)	1.07

*Expected dividend of CY16F+CY17F

	CY16F	CY17F	CY18F
Revised	9.71	10.24	10.90
Previous	9.13	9.53	9.68
Change	6.4%	7.5%	12.6%

Source: IMS Research

NBP vs. KSE100 Index



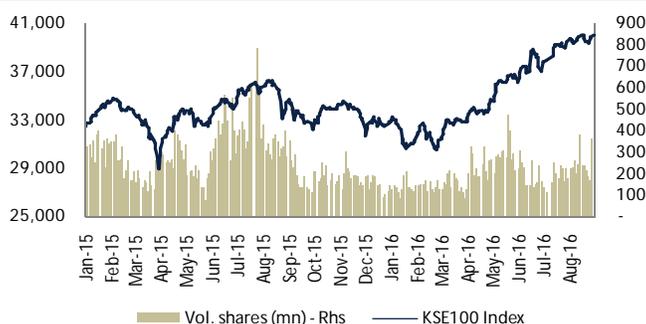
Source: IMS Research

Analyst certification and required disclosures begin on page 3 & 4

To find our Research on Bloomberg, please type - *IMKP <GO>*

Morning News

- **Bank payment agreement to be signed between SBP and Iranian Central Bank:** SBP has shared a draft agreement with GoP for the much awaited BPA with Bank Markazi Jamhuri Iran. According to the draft, both central banks will issue Letter of Comfort to the commercial banks on both sides on individual requests. This will help smooth and expand the bilateral trade between the two countries as absence of banking channel was the key hurdle in payment mechanism for bilateral trade.
- **Shell to add 15 more outlets to its portfolio:** Shell Pakistan has decided to revamp its network of 780 outlets and launch a Shell Select Program, which entails setting up convenience stores and other services on the outlets. Moreover the company is planning to add another 15 outlets to the existing portfolio.
- **Centre and Sindh to reach settlement on power bills soon:** Federal and Sindh government are set to resolve the long outstanding power dues of PKR72bn. According to GoP, Sukkur Electric and Power Company (SEPCO) and Hyderabad Electric Supply Company (HESCO) owe the sum to which Sindh government does not agree. The development will help ease the pressure on the massive circular debt in the country.
- **The Abraaj Group considering divesting stake in K-Electric:** The company announced that its majority shareholder was evaluating the possibility of divesting its stake (of up to 66.4%) in the company to Shanghai Electric Power Company Limited.

KSE100 Index & Volume

Source: PSX

World Indices

	Close	DoD Δ	DoD Δ (%)	CYTD Δ (%)	FYTD Δ (%)
Pakistan	39,991.8	-31.2	-0.1%	21.87%	5.84%
China	3,074.7	4.7	0.2%	-13.12%	4.85%
Hong Kong	23,016.1	194.8	0.9%	5.03%	10.68%
India	28,343.0	440.3	1.6%	8.52%	4.41%
Indonesia	5,362.3	-8.4	-0.2%	-12.10%	6.89%
Malaysia	1,681.6	0.0	0.0%	-0.64%	2.15%
Japan	16,725.4	-12.1	-0.1%	-12.13%	6.65%
Singapore	2,828.4	-1.0	0.0%	-1.89%	-0.63%
Korea	2,039.7	7.4	0.4%	4.00%	2.64%
Taiwan	9,110.6	0.4	0.0%	9.26%	4.26%
Bangladesh	4,534.0	0.0	0.0%	-2.06%	0.59%
Sri Lanka	6,540.2	0.0	0.0%	-5.14%	4.09%
Philippines	7,794.9	-50.6	-0.6%	12.12%	-0.45%
Thailand	1,546.1	2.0	0.1%	20.04%	7.00%
Vietnam	672.7	3.2	0.5%	16.17%	5.06%
USA	2,176.1	-4.3	-0.2%	6.47%	3.48%
UK	6,820.8	-17.3	-0.3%	9.27%	3.69%
Germany	10,657.6	113.2	1.07%	-0.79%	9.02%

Source: Bloomberg

Forex & Money Market

	Close	DoD Δ	YoY Δ bps	CYTD Δ bps	FYTD Δ bps
6m Tbill yield (%)	5.88	0.00	-1.07	-0.51	-0.01
10Y PIB yield (%)	7.78	0.00	-1.60	-1.55	0.19
6m Kibor (%)	5.78	-0.01	-1.04	-0.48	-0.03

	Close	DoD Δ	DoD Δ (%)	YoY Δ (%)	CYTD Δ (%)	FYTD Δ (%)
PkR/US\$	104.82	-0.009	-0.01%	0.8%	0.1%	0.0%
PkR/EUR	117.12	-0.178	-0.15%	-0.2%	2.4%	0.3%
PkR/JPY	1.024	-0.002	-0.20%	19.0%	17.7%	0.4%

Source: Bloomberg

Commodity Prices

	Close	DoD Δ	DoD Δ (%)	YoY Δ (%)	CYTD Δ (%)	FYTD Δ (%)
Gold - US\$/oz	1,311.11	-12.39	-0.9%	15.7%	23.5%	-0.8%
Oil (WTI)- US\$/bbl	46.35	-0.63	-1.3%	2.5%	25.1%	-4.1%
Cotton US\$/lb	65.97	-0.72	-1.1%	3.5%	4.3%	5.0%
Coal - US\$/MT	66.25	0.15	0.2%	22.5%	36.7%	13.2%
CRY Index	182.82	-1.61	-0.9%	-7.2%	3.8%	-5.1%

Source: Bloomberg

Portfolio Flows

(US\$m)	Current	WTD	MTD	12M	CYTD	FYTD
Total FIPI	(0.04)	0.03	0.03	(20.21)	(177.35)	(37.89)
Individuals	4.35	0.36	3.26	56.88	32.26	(43.41)
Companies	(2.79)	(5.39)	5.04	(135.95)	(140.37)	8.47
Banks / DFI	(2.07)	(4.93)	(6.11)	(60.81)	(70.60)	(44.33)
NBFC	0.07	(0.40)	7.50	183.14	141.95	17.60
Mutual Funds	2.52	15.75	15.87	95.04	67.37	71.50
Other Organization	(0.30)	(1.41)	(2.42)	48.96	24.78	(3.56)
Broker Trading	(1.74)	(4.00)	(2.93)	(9.91)	(17.49)	(9.32)

Source: NCCPL

I, Abdul Ghani Fatani, certify that the views expressed in the report reflect my personal views about the subject securities. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations made in this report. I further certify that I do not have any beneficial holding of the specific securities that I have recommendations on in this report.

Ratings Guide*	Total Return
Buy	More than 15%
Neutral	Between 0% - 15%
Sell	Below 0%

*Based on 12 month horizon unless stated otherwise in the report. Total Return is sum of any Upside/Downside (percentage difference between the Target Price and Market Price) and Dividend Yield.

Valuation Methodology: We use multiple valuation methodologies in arriving at a Target Price including, but not limited to, Discounted Cash Flow (DCF), Dividend Discount Model (DDM) and relative multiples based valuations.

Risks: (i) Greater than expected growth in NPLs, (ii) extension of lackluster loan growth trend, and (iii) continuation of high cost-to-income.

Disclaimer: Intermarket Securities Limited has produced this report for private circulation only. The information, opinions and estimates herein are not direct at, or intended for distribution to or use by, any person or entity in any jurisdiction where doing so would be contrary to law or regulation or which would subject Intermarket Securities Limited to any additional registration or licensing requirement within such jurisdiction. The information and statistical data herein have been obtained from sources we believe to be reliable where such information has not been independently verified and we make no representation or warranty as to its accuracy, completeness and correctness. This report makes use of forward looking statements that are based on assumptions made and information currently available to us and those are subject to certain risks and uncertainties that could cause the actual results to differ materially. No part of the compensation of the author(s) of this report is related to the specific recommendations or views contained in this report.

This report is not a solicitation or any offer to buy or sell any of the securities mentioned herein. It is meant for information purposes only and does not take into account the particular investment objectives, financial situation or needs of individual recipients. Before acting on any information in this report, you should consider whether it is suitable for your particular circumstances and, if appropriate, seek professional advice. Neither Intermarket Securities Limited nor any of its affiliates or any other person associated with the company directly or indirectly accepts any liability whatsoever for any direct or consequential loss arising from any use of this report or the information contained herein.

Subject to any applicable law and regulations, Intermarket Securities Limited, its affiliates or group companies or individuals connected with Intermarket Securities Limited directly or indirectly may have used the information contained herein before publication and may have positions in, or may from time to time purchase or sell or have a material interest in any of the securities mentioned or may currently or in future have or have had a relationship with, or may provide investment banking, capital markets and/or other services to, the entities mentioned herein, their advisors and/or any other connected parties.

NOTICE TO US INVESTORS

This report was prepared, approved, published and distributed by Intermarket Securities Limited (IMS) located outside of the United States (a "non-US Group Company"). This report is distributed in the U.S. by LXM LLP USA, a U.S. registered broker dealer, on behalf of IMS only to major U.S. institutional investors (as defined in Rule 15a-6 under the U.S. Securities Exchange Act of 1934 (the "Exchange Act")) pursuant to the exemption in Rule 15a-6 and any transaction effected by a U.S. customer in the securities described in this report must be effected through LXM LLP USA.

Neither the report nor any analyst who prepared or approved the report is subject to U.S. legal requirements or the Financial Industry Regulatory Authority, Inc. ("FINRA") or other regulatory requirements pertaining to research reports or research analysts. No non-US Group Company is registered as a broker-dealer under the Exchange Act or is a member of the Financial Industry Regulatory Authority, Inc. or any other U.S. self-regulatory organization.

Analyst Certification. Each of the analysts identified in this report certifies, with respect to the companies or securities that the individual analyses, that (1) the views expressed in this report reflect his or her personal views about all of the subject companies and securities and (2) no part of his or her compensation was, is or will be directly or indirectly dependent on the specific recommendations or views expressed in this report. Please bear in mind that (i) IMS is the employer of the research analyst(s) responsible for the content of this report and (ii) research analysts preparing this report are resident outside the United States and are not associated persons of any US regulated broker-dealer and that therefore the analyst(s) is/are not subject to supervision by a US broker-dealer, and are not required to satisfy the regulatory licensing requirements of FINRA or required to otherwise comply with US rules or regulations regarding, among other things, communications with a subject company, public appearances and trading securities held by a research analyst account.

Important US Regulatory Disclosures on Subject Companies. This material was produced by Analysis of IMS solely for information purposes and for the use of the recipient. It is not to be reproduced under any circumstances and is not to be copied or made available to any person other than the recipient. It is distributed in the United States of America by LXM LLP USA and elsewhere in the world by IMS or an authorized affiliate of IMS. This document does not constitute an offer of, or an invitation by or on behalf of IMS or its affiliates or any other company to any person, to buy or sell any security. The information contained herein has been obtained from published information and other sources, which IMS or its Affiliates consider to be reliable. None of IMS accepts any liability or responsibility whatsoever for the accuracy or completeness of any such information. All estimates, expressions of opinion and other subjective judgments contained herein are made as of the date of this document. Emerging securities markets may be subject to risks significantly higher than more established markets. In particular, the political and economic environment, company practices and market prices and volumes may be subject to significant variations. The ability to assess such risks may also be limited due to significantly lower information quantity and quality. By accepting this document, you agree to be bound by all the foregoing provisions.

LXM LLP USA assumes responsibility for the research reports content in regards to research distributed in the U.S. LXM LLP USA or its affiliates has not managed or co-managed a public offering of securities for the subject company in the past 12 months, has not received compensation for investment banking services from the subject company in the past 12 months, does not expect to receive and does not intend to seek compensation for investment banking services from the subject company in the next 3 months. LXM LLP USA has never owned any class of equity securities of the subject company. There are not any other actual, material conflicts of interest of LXM LLP USA at the time of the publication of this research report. As of the publication of this report LXM LLP USA, does not make a market in the subject securities.