Banks set to mark highest quarterly core income in 3QCY24E

- We preview 3QCY24 results for Pakistan banks under our coverage, which are expected to report a double-digit growth in core income, potentially at a record-high level as relatively higher decline in funding costs, compared to asset yields, sets stage for sequential expansion in Net Interest Income.
- Despite expected drop in Non-Interest Income not incorporating any one-time gains and continued increase in operating expenses, the higher core income is expected to also take bottom-line at record-high levels on a quarterly basis. This does not include any additional tax pertaining to lower ADR levels.
- Having said that, we expect respective dividend strategies and annual D/Y to remain intact, and not increase during 3QCY24, as the ongoing decline in asset yields are expected to trim future quarterly profits.

3QCY24E: Banks set to mark highest core income…

We preview 3QCY24 results for Pakistan banks under our coverage, which are expected to report a double-digit growth in core income, potentially at a record-high level.

While secondary market yields reflected a volatile trend in the past months, the quarter's averages settled close to preceding quarter. On the other hand, the monetary easing initiation (after 4 years) has brought down deposit rates and borrowing rates for banks as they are tied to the movement in Policy Rates. The impact of the 2.5% Policy Rate cut cumulatively announced in Jun and Jul would have a positive impact on the sector's deposit and borrowing cost. Moreover, the 2% cut announced towards the end of 3QCY24 will broadly be applicable from 4QCY24.

These factors are likely to expand spreads as cost of funds move notably lower to asset yields, in contrary to remaining close to asset yields during 1Q and 2QCY24.

…with sector's NII up 16% QoQ

We expect Net Interest Income (NII) for the sample base to expand 22%/16% QoQ/YoY. Alongside, we expect NIMs to expand 70bp QoQ, however, contract 75bp on a YoY basis. Despite a YoY trim in NIMs, the core income expansion is supported from expected 27% YoY asset base growth, driven by 17% YoY deposits growth and 70% YoY jump in Borrowings.

Other income growth may offset cost growth

On the non-interest income end, we expect pace of higher growth in Fee Income to relatively soften, clocking in at 17% YoY, compared to recent average of 25% YoY, while normalized gain on sale of securities and stable FX income may lead to the secondary income stream to report a sequential decline.

Ongoing disinflation trend may slower the pace of rise in operating expenses, taking Cost to Income ratio back to below 40% (1QCY24: 43%). Moreover, we also prudently built in higher provision expenses for the quarter assuming impact of macro conditions on the quality of the sector's loan portfolio.

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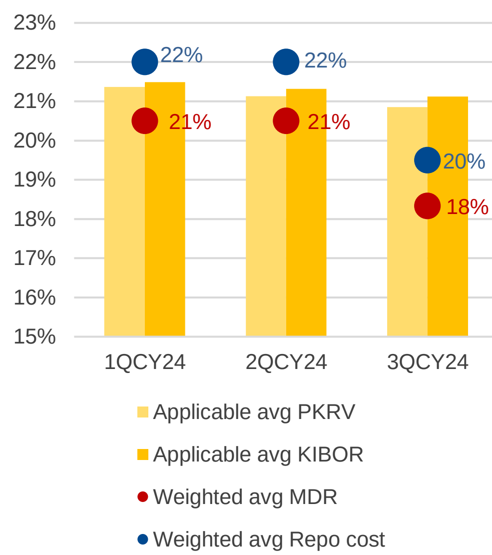
Banks: Estimated yield & cost movement



Source: SBP, MUFAP, JS Research

On taxes front, standard corporate tax of 39% and Super Tax for the quarter at 10% is expected to keep effective tax rate at 49%. We do not factor in the penal tax on lower ADR, the practice followed in 1HCY24 by the sector despite lower ADR levels as we believe banks would either meet ADR targets by year end or book relevant taxes pertaining to the same in annual results.

JS Banking Universe: 3QCY24 Earnings preview

Rs.	EPS					DPS	
	3QCY24E	YoY	QoQ	9MCY24E	YoY	3QCY24E	9MCY24E
HBL	10.30	-9%	5%	30.47	4%	4.00	12.00
UBL	14.99	24%	24%	40.14	18%	11.00	33.00
MCB	14.97	-10%	6%	44.18	9%	9.00	27.00
ABL	9.70	-1%	-10%	30.33	21%	4.00	12.00
BAHL	12.06	20%	21%	31.04	18%	3.50	10.50
MEBL	16.87	17%	13%	45.98	40%	7.00	21.00
BAFL	6.12	12%	-10%	19.19	11%	3.00	7.00
AKBL	3.95	0%	31%	9.52	-5%	0.00	0.00
HMB	6.00	-15%	12%	16.97	-7%	3.00	8.00
FABL	5.29	78%	19%	14.04	77%	2.00	5.00

Source: JS Research

Higher yields to further boost adequacy levels

The movement in secondary market yields is expected to result in increasing outstanding unrealized gains / recovery in outstanding losses under the Surplus of Revaluation on Available for Sale fixed rate securities as yields have witnessed a sharp decline QoQ.

To recall, unrealized Loss on Available for Sale Securities for our banking universe turned into cumulative gains during 2QCY24 (from loss of Rs25bn to gain of Rs42bn), supporting sector's overall adequacy levels. Higher profits for 3QCY24, would further boost sector's CET-I buffer. Having said that, we expect respective dividend strategies and annual D/Y to remain intact, and not increase, as the ongoing decline in yields are expected to trim future quarterly profits.

Secondary market yields movement

	2QCY24 end	3QCY24 end	*QoQ*
3M	20.0%	15.5%	*-4.5%*
6M	19.9%	14.6%	*-5.3%*
12M	18.7%	13.5%	*-5.2%*
3YR	16.5%	12.3%	*-4.2%*
5YR	15.4%	12.2%	*-3.2%*
10YR	14.1%	12.1%	*-2.0%*

Source: MUFAP, JS Research

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