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Banks & rising bond yields

Banks with higher fixed rate PIBs & duration to be affected

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Impact of rising yields on Banks

- After an unexpected increase in cut-off yields in last T-Bill auction on Dec 1, 2021, money market yields have been on a rising trend recently.
- Bond yields are up 136-144bps since SBP increased the policy rate by 150bps on Nov 19, 2021. Since the last PIB auction on Nov 29, 2021, bond yields on 3-5 year PIBs are up around 50bps to 11.89% and 11.91%, respectively. In 2021 to date, bond yields on 3-5 years bonds are up 362bps and 266bps, respectively. This is on expectations of further rate hike going forward on the back of rising inflationary pressures and import bill.
- We believe this development can have implication on Pakistan's banking sector. As per our calculations and channel checks, around 46% of our sample bank's investments is in PIBs whereas around 18% of the investment is in fixed coupon PIBs.
- We believe that banks with higher fixed rate PIBs and duration will be losers in such a scenario as their rates are locked in for higher duration in an increasing interest rate scenario as it will impact their net interest margins and profitability. Our channel checks suggests that the average duration of sample banks for fixed rate PIBs is around 2-3 years and their investments is locked in at an average of 8-10% compared to current yields of ~12%.
- On other hand, banks with higher current account deposits, higher T-Bill & advances concentration and lower fixed rate PIBs/duration are likely to be gainers in rising interest rates.
- Furthermore, rise in bond yields could also result in revaluation losses for banks on investments classified as 'Available for sale Investments (AFS)' as bond prices and bond yields are inversely related. This may not only impact bank's equity/book value but may also result in lower capital adequacy ratios (CAR) for the banks.
- We maintain our 'Overweight' stance on the banking sector with MEBL, MCB and UBL as our top picks.

Topline Universe Bank Fixed Coupon PIB Holdings (as of Sep 30, 2021)

Amount (Rsbn)	PIBs	Fixed Coupon PIBs	Deposits	Fixed PIB as % of Total PIB	Fixed PIBs as % of Total Deposits	ADR	Fixed PIBs as % of Total Investments	Fixed PIBs as % of Total Equity
BAFL*	394	100	1,036	25%	10%	62%	14%	108%
NBP**	620	250	2,552	40%	10%	40%	12%	86%
UBL*	655	244	1,810	37%	13%	31%	16%	131%
HBL*	1,050	470	3,167	45%	15%	43%	24%	167%
MCB	607	234	1,457	39%	16%	33%	20%	132%
BAHL*	536	241	1,273	45%	19%	52%	26%	274%

Source: Company Accounts, Topline Research

*Fixed Coupon PIB amounts shared in accounts or Corporate Briefing session of respective banks, **channel checks

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