

Sri Lanka Listed Banking Sector Performance- 1H'24

ECONOMIC STABILITY & RECOVERY ARE EXPECTED TO TAKE CENTERSTAGE POST ELECTIONS. BANKS TO ALIGN WITH BROADER ECONOMIC RECOVERY

CURRENT VALUATIONS OF BANKS PRESENT ATTRACTIVE OPPORTUNITY TO ENTER THE MARKET

- We expect economic recovery to continue irrespective of the election outcome as all candidates are aware of the importance of stabilizing the economy especially economic recovery and long-term fiscal stability. All candidates seem to be showing commitment to address the financial challenges and while appealing to the voters there is a growing recognition of the need for sustainable economic policies . We also think while there may be negotiations for modifications, the new administration will have limited room to deviate from the current economic agreement with IMF, as each candidate is aware that continuity is crucial for maintaining economic stability.
- The Colombo Stock Exchange (CSE) is currently trading at relatively low multiples, reflecting undervaluation in several key sectors, despite multiple catalysts that suggest potential for significant growth ahead.
- With the International Sovereign Bond (ISB) restructuring doubts are been largely resolved and the overhang of uncertainty around debt sustainability has been addressed, we expect the sector to move on with renewed confidence . Low-cost borrowings should spur loan book growth in the coming quarters benefiting banking sector counters and coupled with the overall recovery in the economy should help reduce nonperforming loans.
- Banking sector counters are currently trading at historical low multiples and at a significant discount to their book value, therefore providing attractive entry points for long term investors in our view.

SRI LANKA BANKS: LICENSED COMMERCIAL
BANKS (LCB) : KEY PERFORMANCE
INDICATORS 1H’24

Total Assets of LCB’s
LKR 18.7 Tn
As at 30.06.2024

Net Loan Book of LCB’s
LKR 9.2 Tn
As at 30.06.2024

Loan Book Growth
5.5% YoY
As at 30.06.2024

Deposit Book of LCB’s
LKR 15.0 Tn
As at 30.06.2024

Deposit Book Growth
+8.7% YoY
As at 30.06.2024

Stage 3 Loans
12.9%
As at 30.06.2024

Avg NIMS
3.9%
As at 30.06.2024

Avg ROE (after tax)
12.6%
As at 30.06.2024

Stage 3 Impairment Coverage
52.4%
As at 30.06.2024

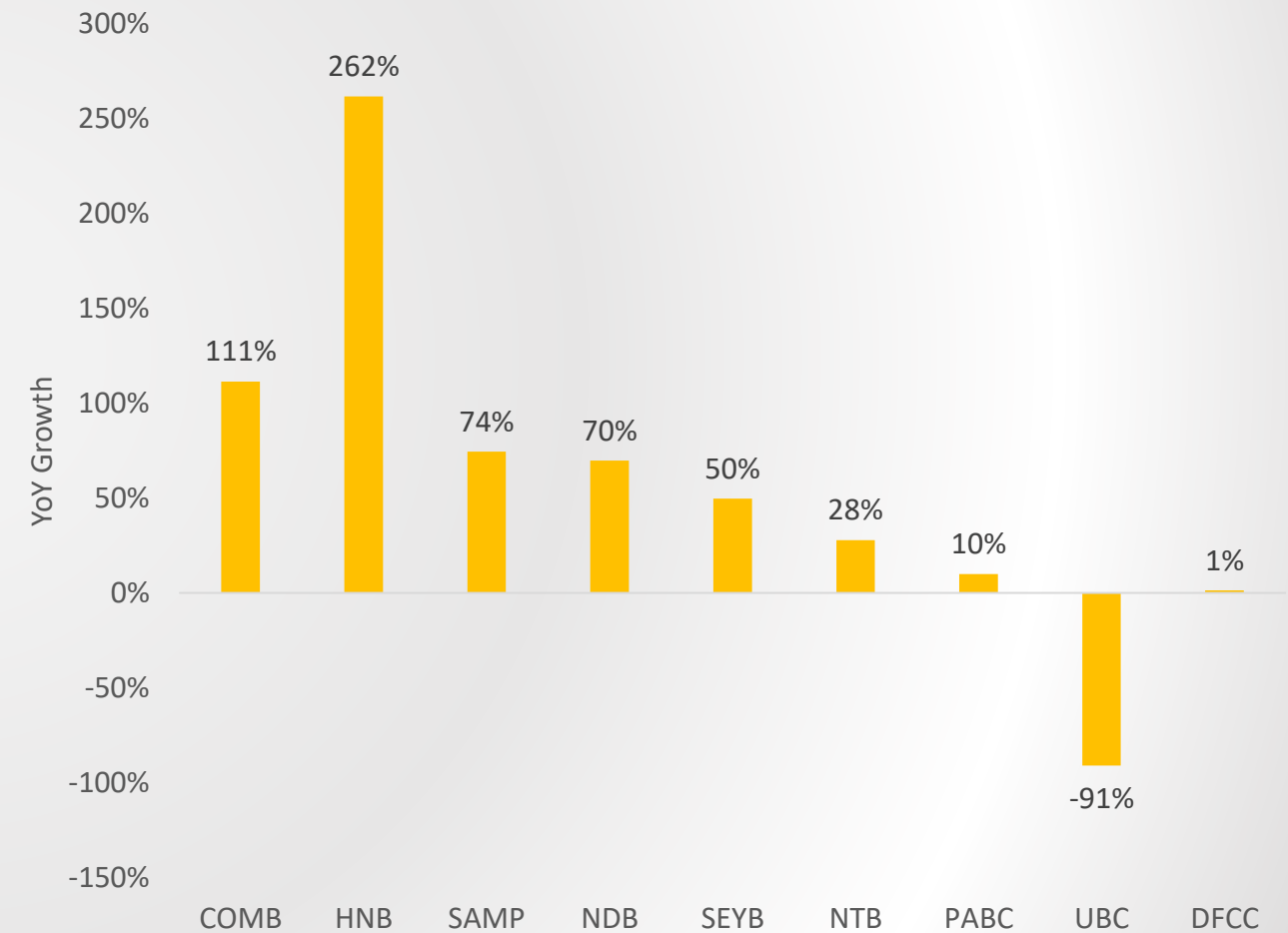
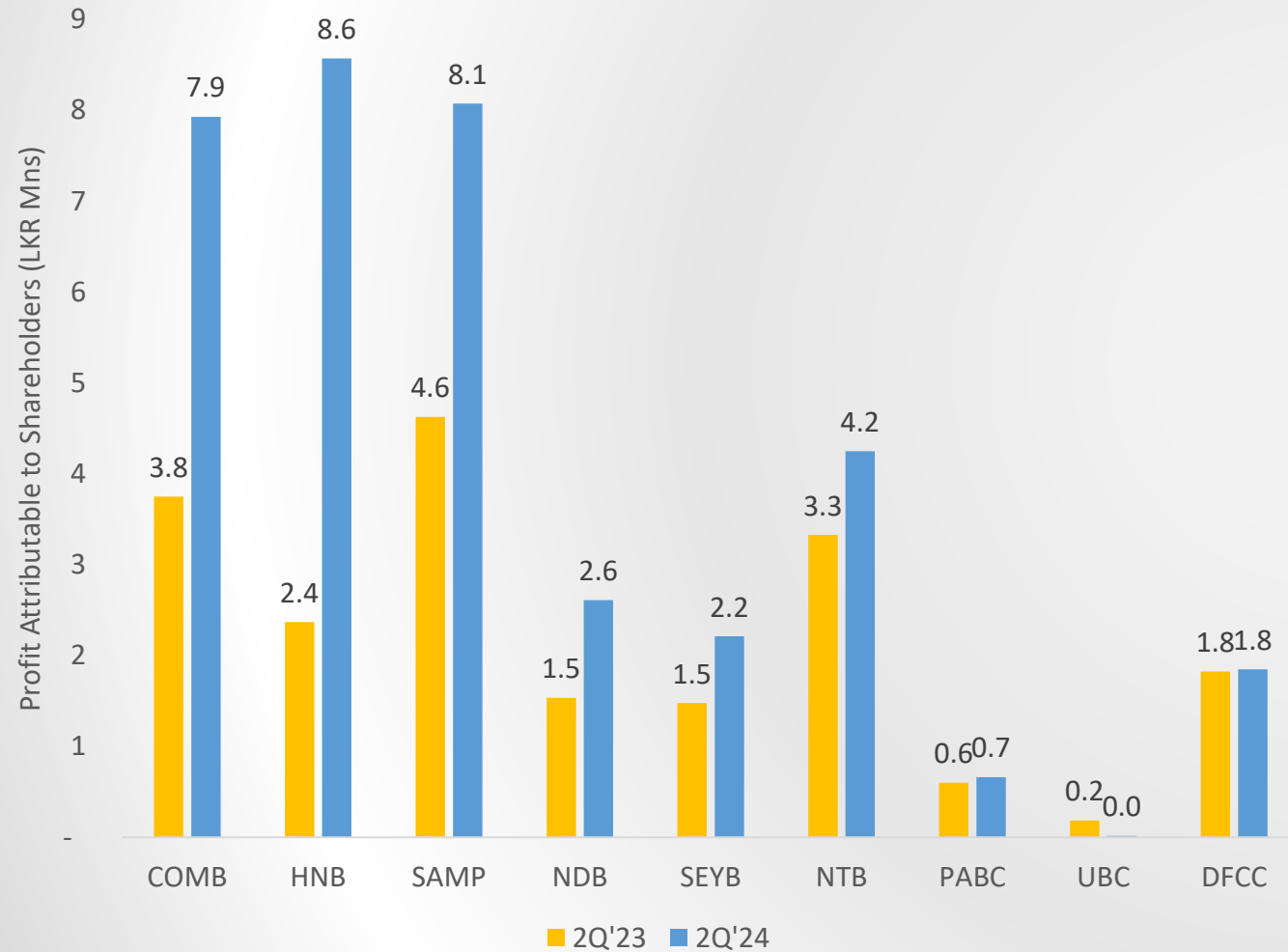
Tier 1 Capital Ratio
14.7%
As at 30.06.2024

CASA Ratio
32.5%
As at 30.06.2024

Avg Banking Sector PE/PVB
PE-3.7X, PVB-0.5X
As at 19.09.2024

BANKS RECORDED EXCEPTIONAL PROFITS BACKED BY HIGHER NII & LOWER IMPAIRMENTS

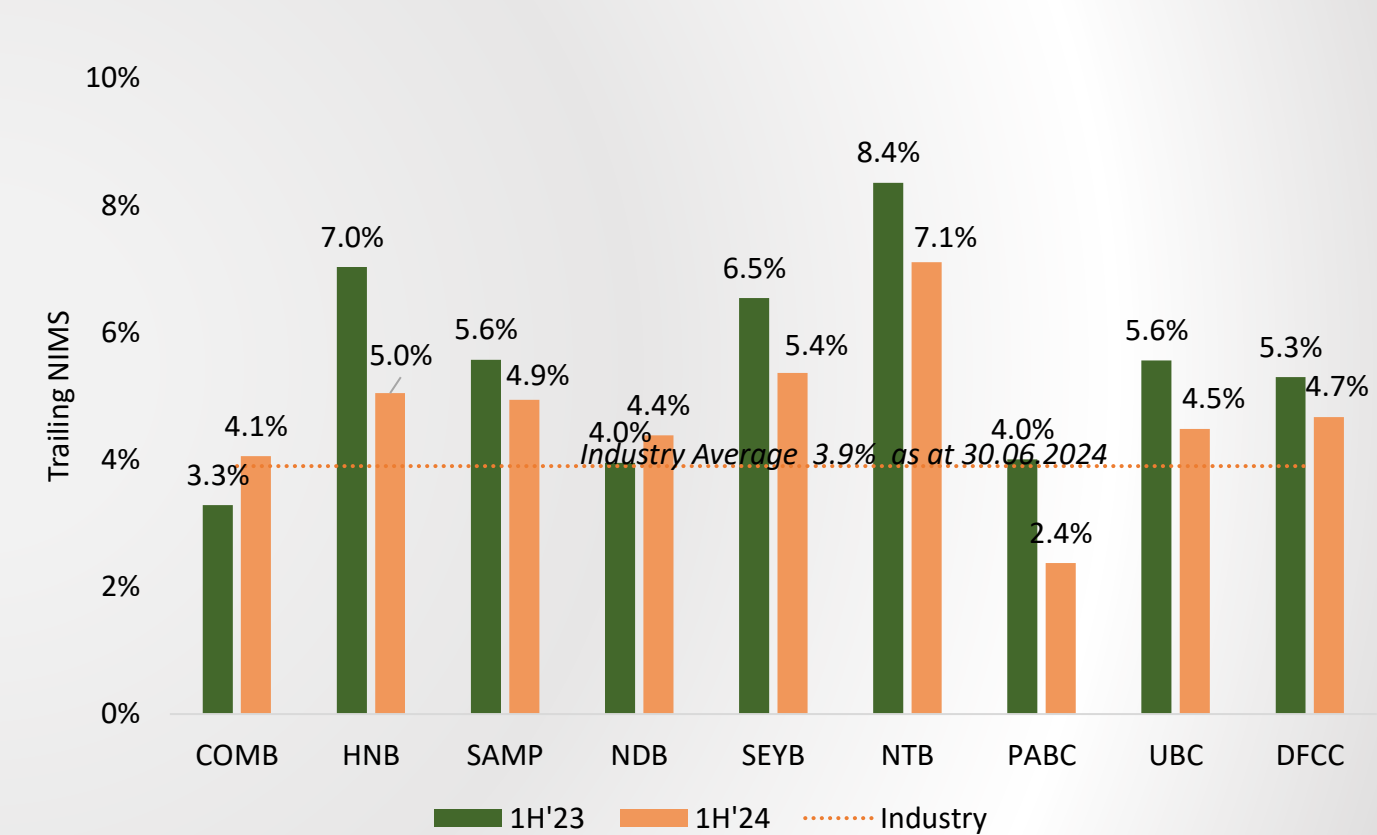
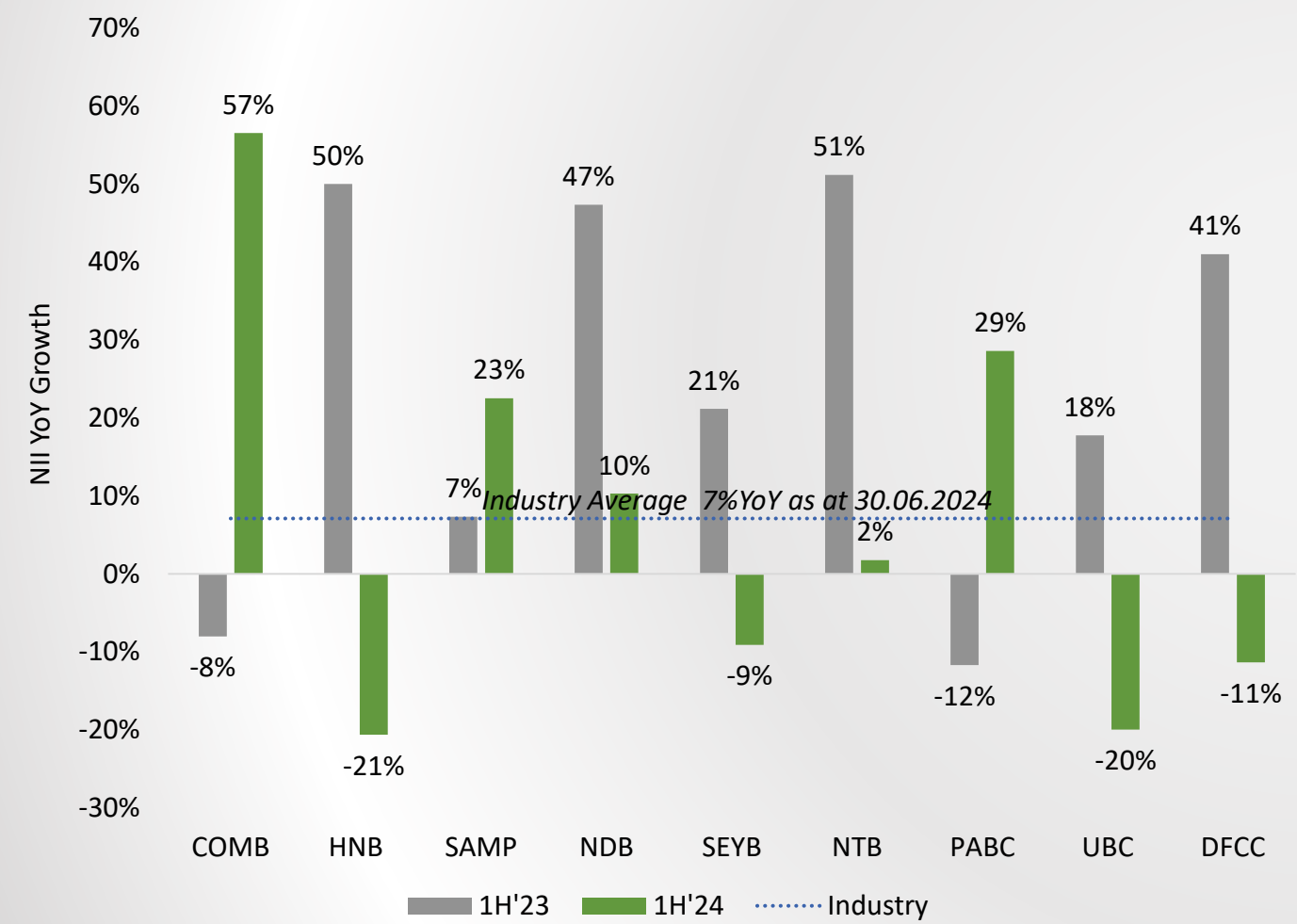
HNB RECORDED THE HIGHEST PROFITS FOLLOWED BY SAMP AND COMB FOR 2Q'24



COMB- Commercial Bank, HNB-Hatton National Bank, SAMP- Sampath Bank, NDB- National Development Bank, SEYB- Seylan Bank, NTB- Nations Trust Bank, PABC- Pan Asia Bank, UBC- Union Bank, DFCC- DFCC Bank,

NII IMPROVED IN MANY BANKS WITH DECREASE IN INTEREST EXPENSE, OUTPACING THE DECLINE IN INTEREST INCOME

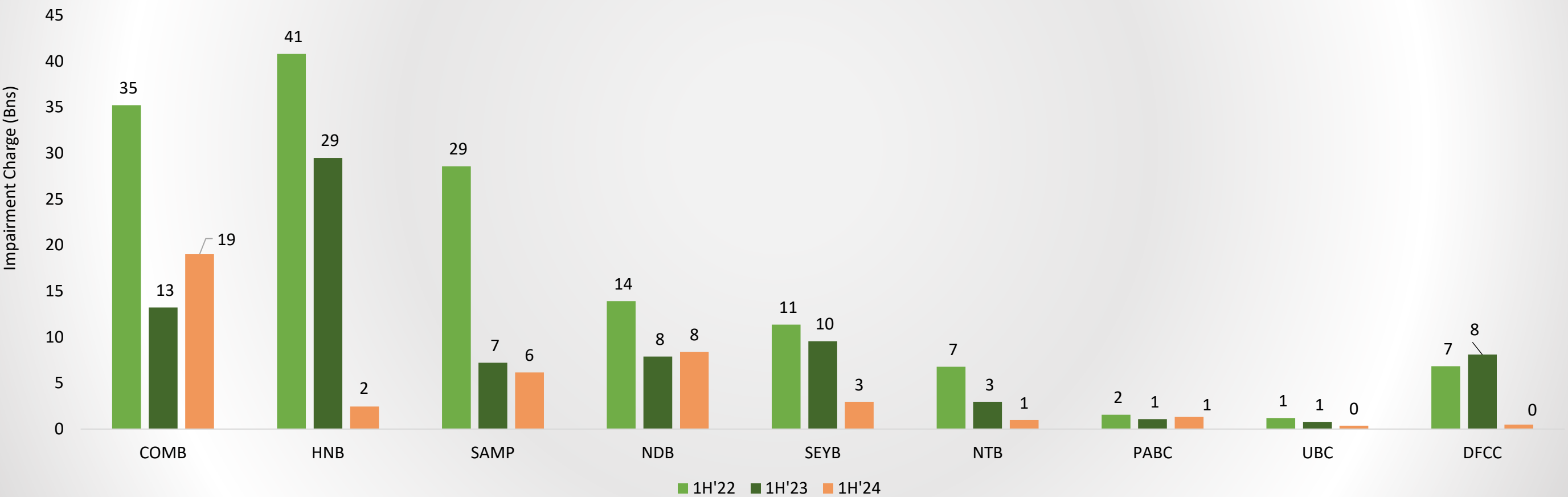
NIMS HENCE SAW EXPANDING OR COMING DOWN AT A SLOWER PACE



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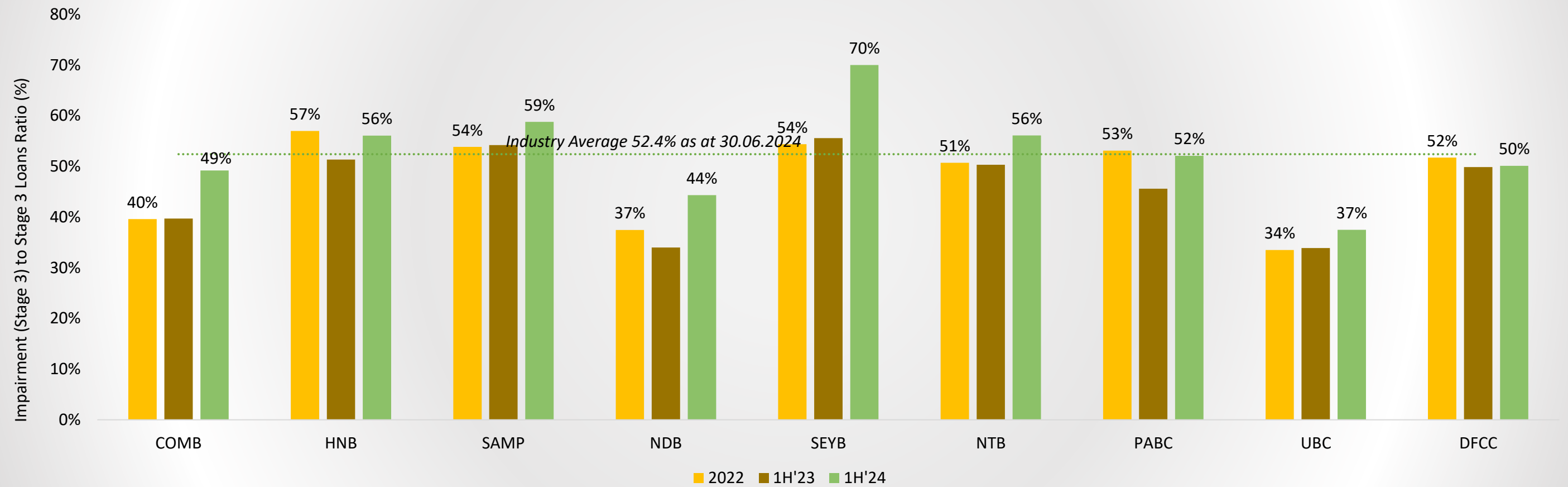
IMPAIRMENTS LARGELY REDUCED WITH REDUCTION IN PROVISIONS FOR ISBS.

IMPROVEMENT IN COLLECTIONS AND RECOVERY TOO HELPED IN REDUCING THE PROVISIONING



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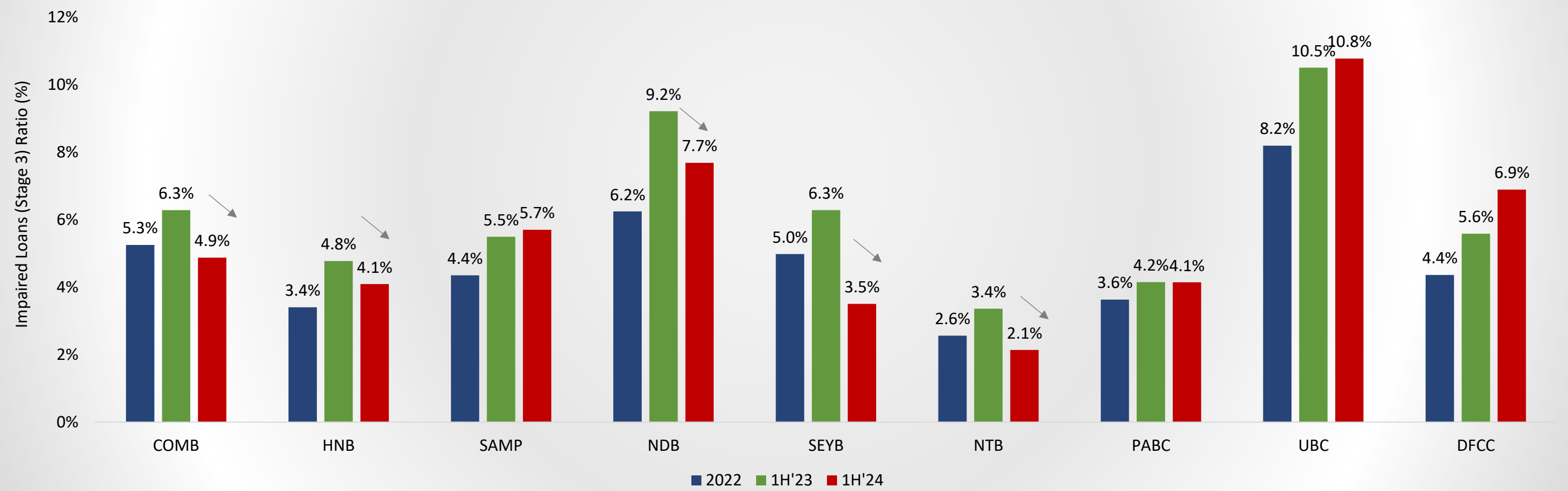
COVERAGE RATIOS OF ALL BANKS HAVE ALSO EDGED UP
ADDITIONAL COVERAGE WAS BUILT FOR RISK-ELEVATED SEGMENTS IN THE LOANS AND ADVANCES PORTFOLIO.



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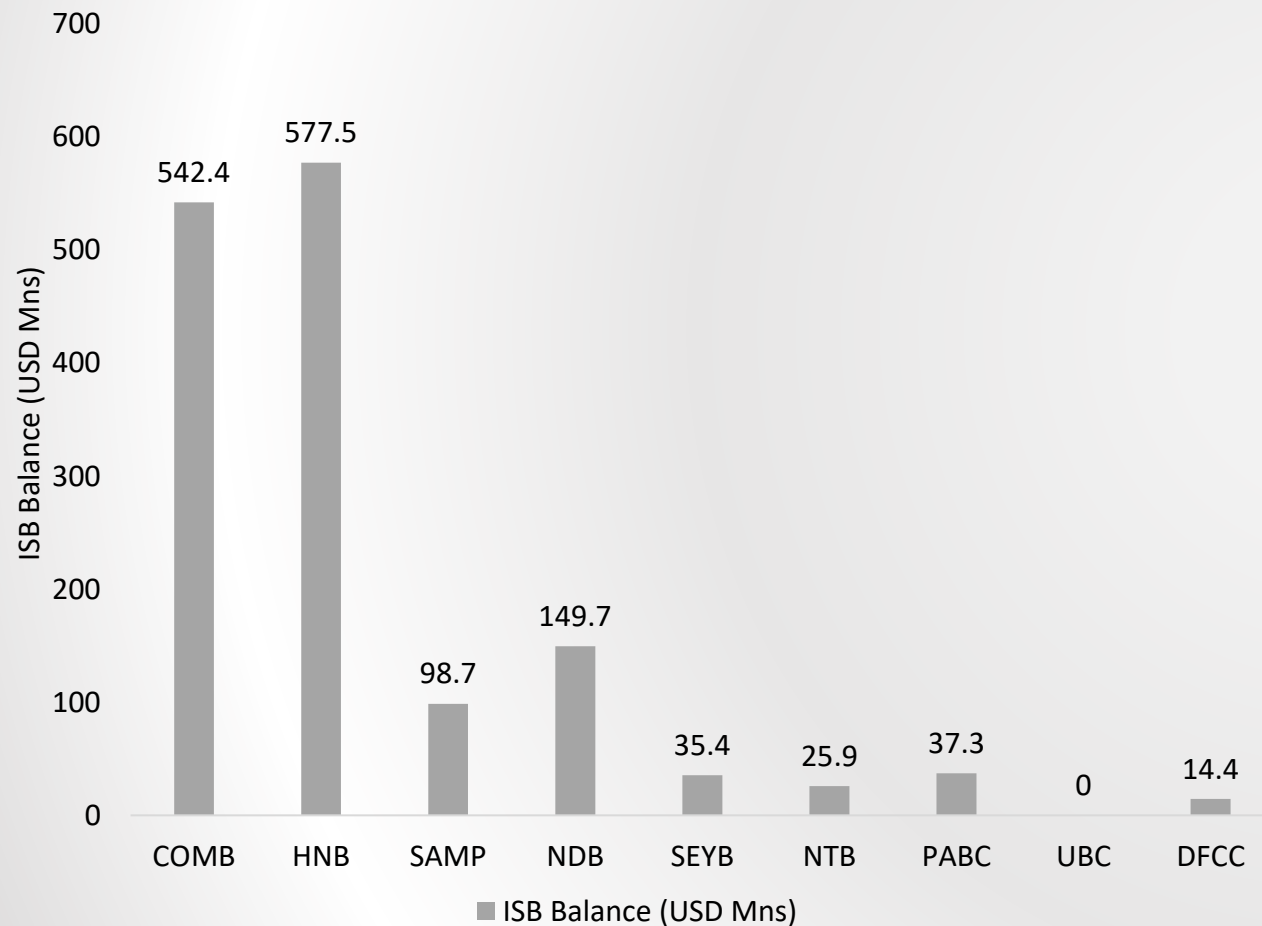
STAGE 03 IMPAIRMENT LOANS TAPERED DOWN SIGNALING GRADUAL PROGRESS IN MACRO INDICATORS

STAGE 03 IMPAIRED LOANS SHOULD SLOW DOWN FURTHER WITH ECONOMIC CONDITIONS IMPROVING



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BANKS WHICH HAS A HIGH EXPOSURE TO FOREIGN INSTRUMENTS TO SEE SIGNIFICANT REVERSALS WITH THE PROPOSED DEBT RESTRUCTURING PLAN

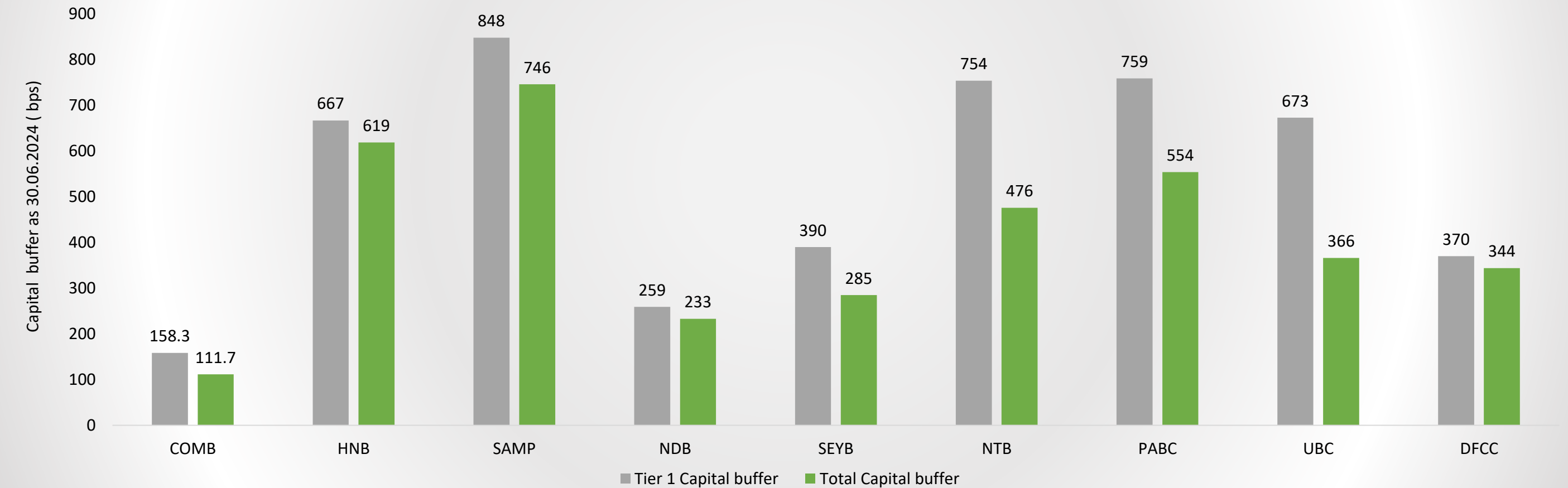


- Banks have the option to exchange 70% of the face value of the outstanding USD bonds with a 10% haircut.
- The remaining 30% can be taken as an LKR bond at floating rate coupon of SLFR +0.5%
- Despite the 10% haircut, coupon reduction for USD bonds will be higher than the baseline scenario, with coupon rates standing around 1%-2% compared to ~ 4% in the baseline scenario.
- LKR bonds meanwhile be matured in 2043(cf. 2038 of USD bonds) with the principal payment scheduled to be in 2036.
- Banks thus could see a significant reversal in provisions particularly since they have already made provisions for a haircut exceeding 50%.

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CAPITAL BUFFERS ARE ADEQUATE TO SUPPORT THE NEXT LEVEL OF GROWTH

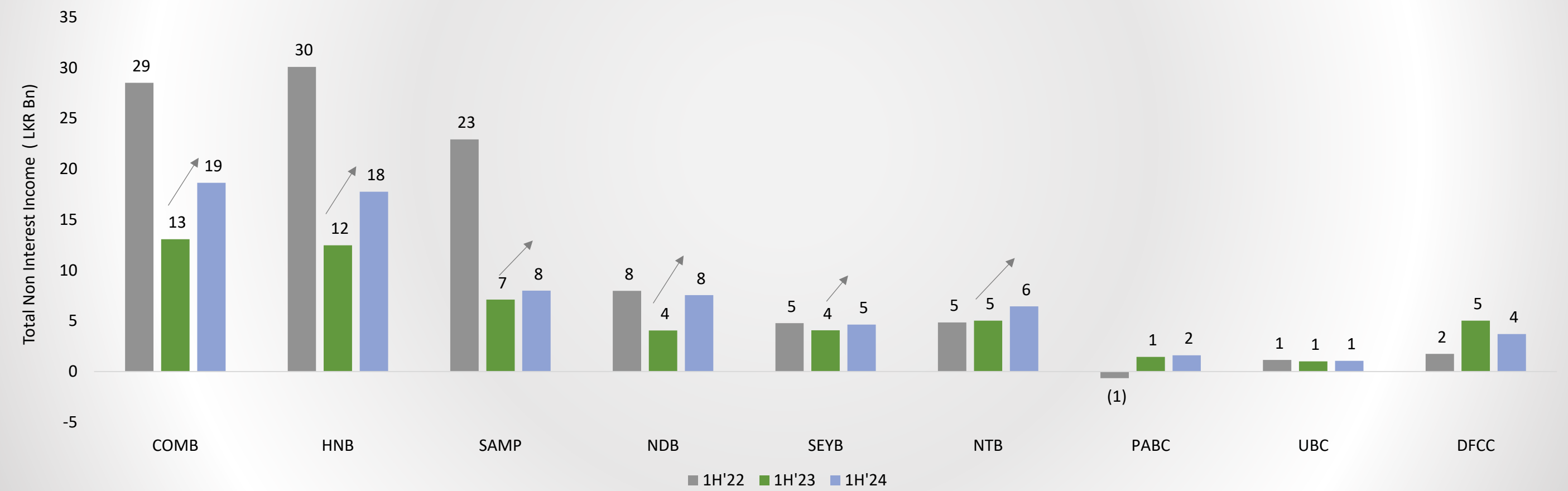
HNB, COMB. NDB & SAMP SHOULD SEE SOME PROVISIONS REVERSING WITH THE NEW RESTRUCTURING FRAMEWORK. COMB’S BUFFER TO INCREASE BY LEAST ANOTHER ~150BPS ALONG WITH THE PROPOSED RIGHTS ISSUE. IMPROVED PROFITABILITY TO ALSO HELP.



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NON-INTEREST INCOME IMPROVED WITH HIGHER FEE INCOME & FOREIGN EXCHANGE TRANSACTIONS

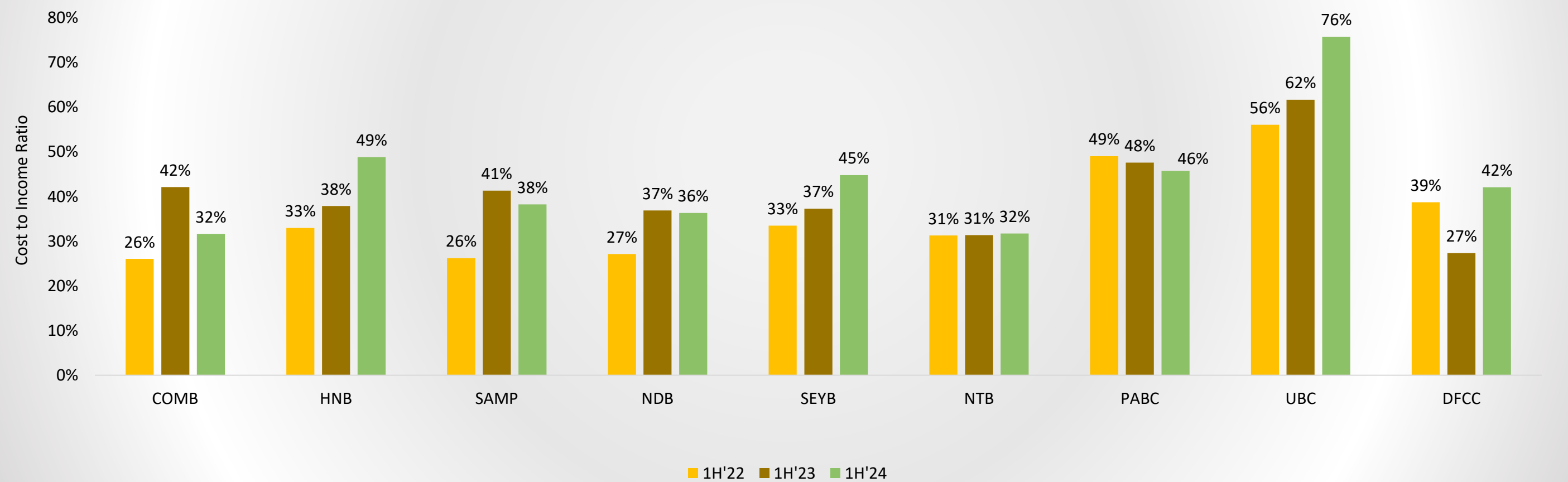
FEE INCOME SHOULD JUMP FURTHER WITH TRADE RELATED ACTIVITIES IMPROVING AND POSSIBLE RELAXATION OF IMPORT RESTRICTIONS



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COUNTERS THAT RECORDED HIGHER NII AND INCREASED NON-INTEREST INCOME EXPERIENCED A SIGNIFICANT DROP IN COST TO INCOME RATIO.

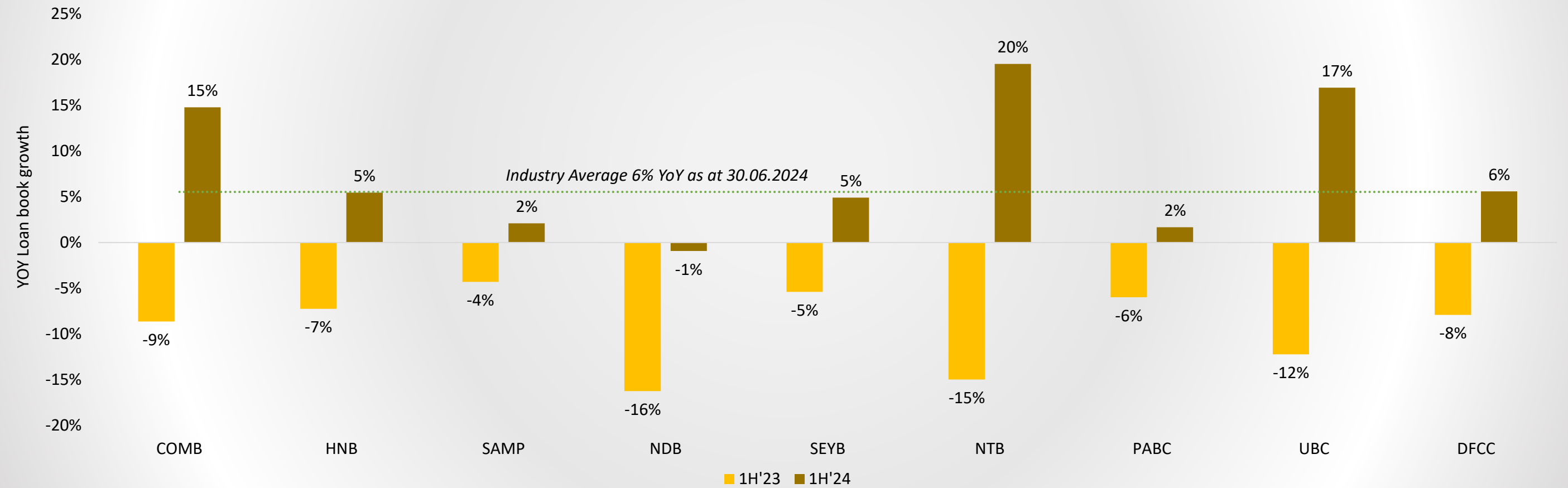
COST BASE TO SEE A MODERATE GROWTH DUE TO SUBDUED INFLATION



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LOAN BOOKS SAW A SHARP UPTICK IN 1H'24 HELPED MAINLY BY IMPROVED ECONOMIC ACTIVITIES

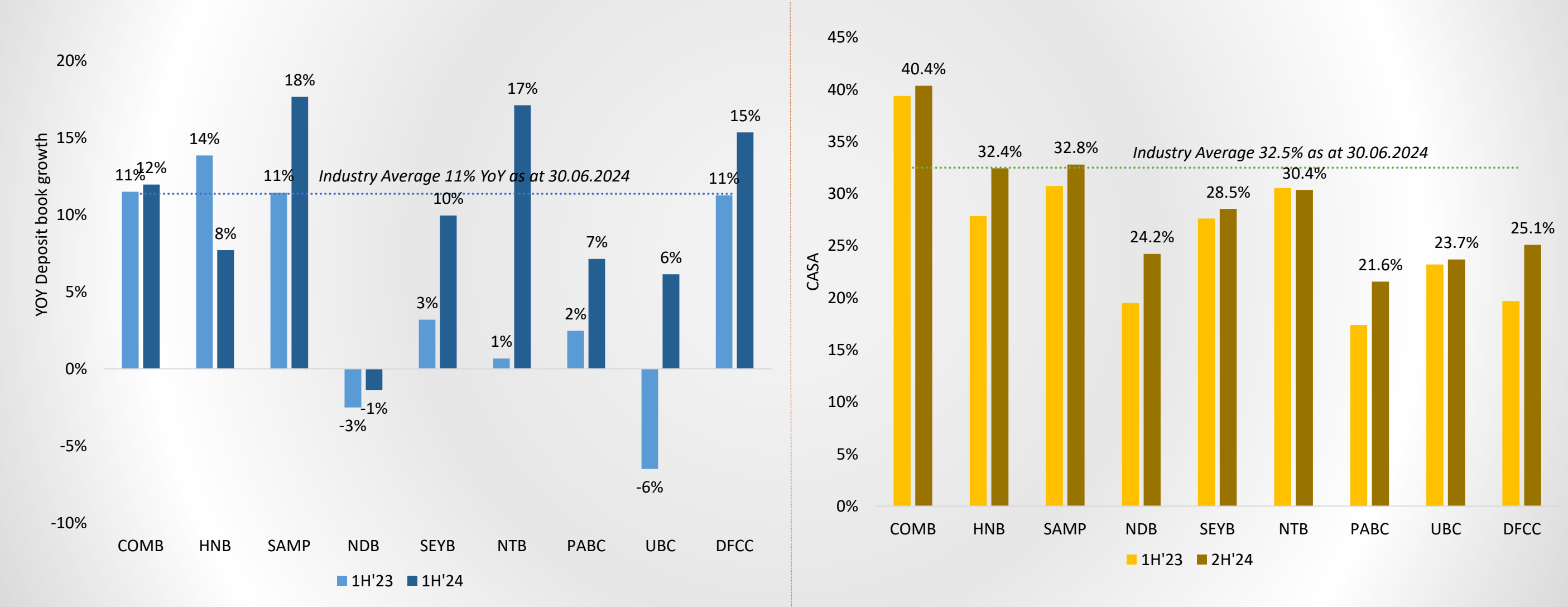
LOW INTEREST RATES AND HIGHER ACTIVITIES TO DRIVE UP THE LOAN BOOKS OF BANKS



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DEPOSIT BOOK ALSO EXPANDED DESPITE FCY DEPOSITS SEEING DECLINING DUE TO LKR APPRECIATION

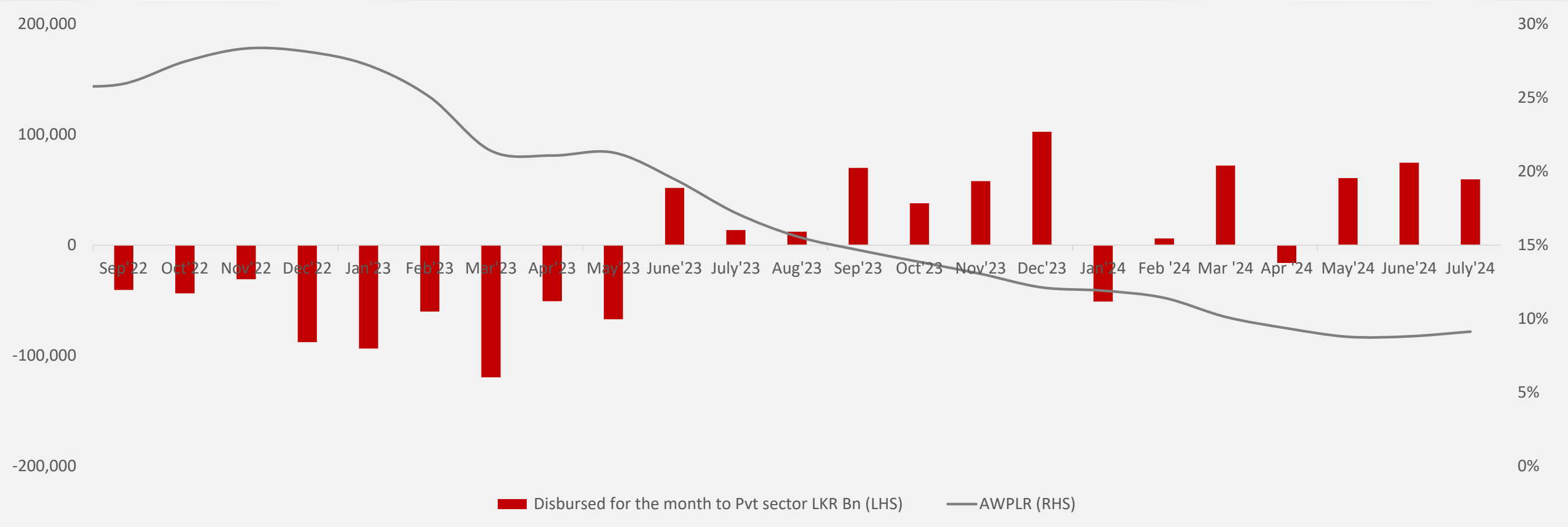
CASA BASE IMPROVED SPECIALLY WITH REPRICING OF DEPOSITS



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PRIVATE SECTOR CREDIT IS ALREADY ON AN UPWARD SWING AND SHOULD MOVE IN TANDEM WITH GDP GROWTH

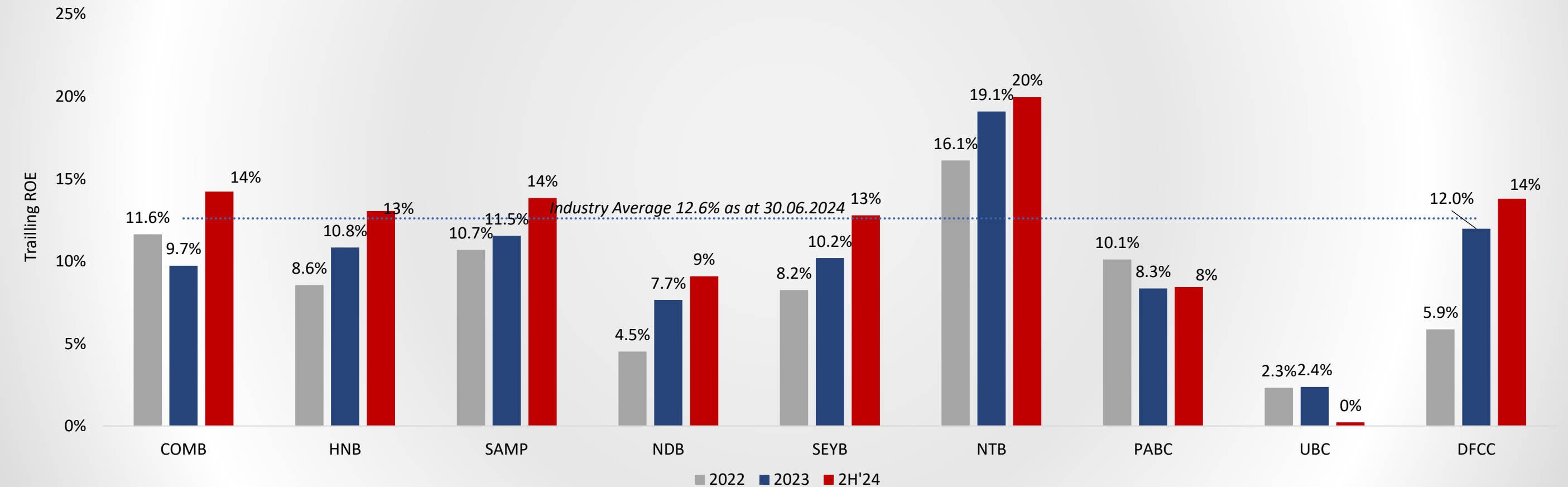
NIMS SHOULD GET STABILIZED AS THE SPREAD IS GETTING WIDER IN THE RECENT PAST



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RETURNS TO MOVE UP AMID IMPROVED PROFITS

HIGHER ACTIVITIES, LOWER IMPAIRMENTS, IMPROVED LOAN BOOK GROWTH , INCREASED FEE INCOME TO DRIVE UP PROFITS



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Banking Sector : Valuations

BANKING SECTOR IS TRADING AT HISTORICAL LOW MULTIPLES

MAKING AN ATTRACTIVE ENTRY POINT FOR LONG TERM INVESTORS

Counter	Ticker	MP as at 19/09/2024	PE (X)	PBV (X)	Trailing DY	ROE (%)
Banking Sector			3.7	0.48		13.0
Commercial Bank	COMB-N-0000	85.00	4.3	0.61	7.6	14.1
Commercial Bank [NV]	COMB-X-0000	71.00	3.6	0.51	6.8	14.1
DFCC Bank	DFCC-N-0000	68.50	2.9	0.39	7.3	13.5
Hatton National Bank	HNB -N-0000	164.25	3.2	0.41	4.9	12.8
Hatton National Bank [NV]	HNB -X-0000	138.75	2.7	0.35	5.8	12.8
HDFC	HDFC-N-0000	31.80	1.1	0.25	na	21.7
National Development Bank	NDB -N-0000	67.90	4.1	0.37	7.4	9.0
Nations Trust Bank	NTB -N-0000	114.25	2.8	0.54	4.4	19.4
Nations Trust Bank [NV]	NTB -X-0000	126.00	0.4	0.60	4.0	19.4
Pan Asia Bank	PABC-N-0000	19.40	4.4	0.37	1.3	8.3
Sampath Bank	SAMP-N-0000	72.20	3.8	0.52	8.1	13.6
Sanasa Development Bank	SDB -N-0000	30.00	8.2	0.34	2.9	4.1
Seylan Bank	SEYB-N-0000	44.80	3.4	0.43	5.6	12.6
Seylan Bank [NV]	SEYB-X-0000	34.40	2.6	0.33	7.3	12.6
Union Bank	UBC -N-0000	9.20	60.5	0.51	na	0.9
Cargills Bank	CBNK-N-0000	7.40	21.6	0.58	na	2.7

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