

## Habib Bank Limited (HBL PA)

### Legal issues remain relevant

A US district court has given a procedural decision in three combined cases against HBL, filed under the Anti-Terrorism Act. All of the primary liability claims against the bank have been dismissed, and the remaining secondary liability claims may yet warrant dismissal on jurisdictional grounds. In the event of the latter, we believe follow-on civil proceedings may be moot. HBL hit its lower circuit today, contributing the most to the KSE100's fall, with local institutions selling the stock down to individuals. HBL has indicated the allegations are without merit, and we believe it looks very cheap on valuations. However, the stock may continue to trade at a discount relative to history and peers until complete clarity emerges. On the flipside, if civil proceedings fail to take place, or if HBL receives a favorable ruling going forward, there is significant room for the stock to rerate.

#### The case

- From 2020 onwards, the United States District Court for the Southern District of New York heard three combined cases against HBL, filed on behalf of 370 individuals injured or killed in terrorist attacks.
- In its procedural decision, the Court has dismissed all primary liability claims against HBL. It has denied the motion to also dismiss claims of secondary liability, but even these may warrant dismissal on jurisdictional grounds where we understand HBL has the room to renew its motion. Follow-on civil proceedings are thus possible but not certain, in our view.
- As per HBL, the allegations are without merit and the bank is contesting them. Secondary liabilities, if any, will be determined after due legal proceedings. The bank has reaffirmed its commitment to AML and CFT protocols.

#### Our take

The following could play out for HBL in the near-term:

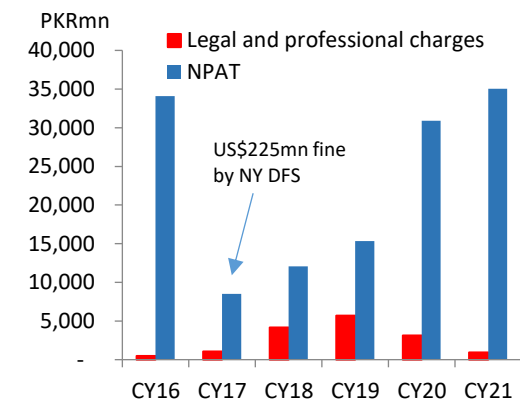
- It is possible that legal and compliance costs increase, but at a much lower quantum compared to 2018/19 when the bank spent heavily to improve its compliance processes and systems in the aftermath of its 2017 fine. Higher than expected expenses may lead HBL to raise additional ADT-1 capital, given its Tier-1 CAR of 12.5% is near the regulatory minimum (HBL is Systemically Important and has to maintain an additional 2% buffer).
- Given its 3.5% weight in the KSE100 Index, HBL is extensively owned by local institutional investors. In addition, as of December 2021, foreign shareholders held more than 10% of HBL's shares. Local institutions aggressively sold HBL today, as the news broke, while buyers were local individuals. It is possible that until complete clarity emerges, a perceived higher risk profile associated with HBL leads to lower institutional holding of the stock than at present.
- On P/B, HBL trades at a steep c 60% discount to its 5yr average P/B multiple. While we last rated HBL a Buy, it is possible that HBL's share price embeds this valuation discount over the course of the potential civil proceedings. On the flipside, if civil proceedings fail to commence, or if HBL receives a favorable verdict going forward, there appears to be significant upside from current levels. The bank has already shed 32% CYTD to trade at a 2023f P/B of 0.35x and P/E of 2.2x.

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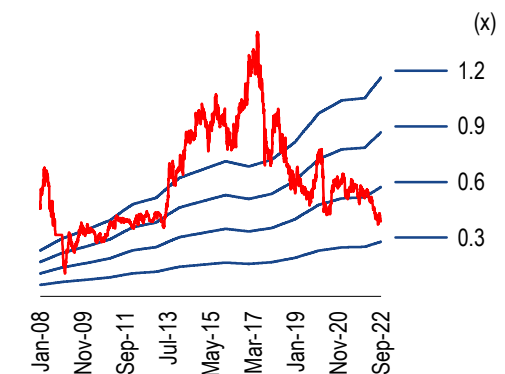
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#### HBL faced a large fine in 2017



Source: Company Accounts, IMS Research

#### P/B is at a c 60% discount to 5 Yr average



Source: IMS Research

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Ratings Guide*	Criteria
Buy	Total return expectation of $\geq 15\%$ or expected to outperform the KSE-100 index
Neutral	Total return expectation of $> -5\%$ or expected to match the return of KSE-100 index
Sell	Expected downside of more than 5% or expected to underperform the KSE-100 index

\*Based on 12 month horizon unless stated otherwise in the report.

**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) Not applicable

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