

Strong activity growth for Alpha banks in the third quarter, driven by domestic activity

The Alpha Report, outlining the performance and positioning of the first 14 banks in Lebanon with deposits exceeding US\$ 2 billion, was issued by Bankdata Financial Services for the third quarter of 2016.

Alpha banks reported a strong consolidated activity growth in the first nine months of 2016, driven mainly by domestic activity. Measured by the consolidated assets, banking activity grew by 5.1% year-to-date, with domestic activity growing by 6.8% and foreign activity regressing by 1.6%. The former was favored by the financial engineering operations of the Central Bank of Lebanon that generated a significant growth in financial inflows to Lebanon estimated at 36% year-on-year over the first nine months of 2016, triggering a corollary increase in domestic customer deposits. The decline in foreign activity is tied to the foreign currency translation effects following the depreciation of the Egyptian Pound and Turkish Lira; Egypt and Turkey being main foreign markets for Lebanese banks in terms of assets.

Customer deposits that account for 81% of banking activity followed the same pace, with domestic deposits growing by 4.3% and foreign deposits contracting by 2.0%. It is worth mentioning that the currency breakdown of domestic deposits puts forward that LL deposits grew by 3.7% and FX deposits rose by 4.7%, keeping deposit dollarization at its level of 63.6% at end-September 2016. It is worth also noting that the year 2016 did not witness any branch network expansion but added 403 employees to raise total staff employed to 31,148 employees, of which 68% in Lebanon and 32% abroad.

The analysis of Alpha banks' lending portfolios suggests a strong lending growth of 4.7% over the first nine months of 2016, with domestic lending growing by 3.9% and foreign lending rising by 6.5%. The noticeable development in domestic lending was the lending in LL that grew by a significant 9.4%, thus contracting lending dollarization to a new low. We are witnessing a gradual restoration of the role of the Lebanese Pound as a borrowing currency. The growth in lending activity was not realized at the detriment of asset quality, as gross doubtful loans as a percentage of total loans stabilized at 5.72% (6.66% when including substandard loans), close to its level a year ago. With a coverage ratio of 74.43% of loan loss reserves to doubtful loans, the net doubtful loans to gross loans remain low at 1.46%. Most importantly, collective provisions as a percentage of net loans reached a record high of 1.27% by end-September 2016. In parallel, banks took significant collective provisions prior to IFRS 9 implementation within the context of BDL directives following its special transactions in the third quarter of the year.

Net Primary liquid assets constituted 33.58% of customer deposits in September 2016, further raising the ratio in comparison with the emerging markets average of circa 22%, suggesting that Alpha banks remain highly liquid on the overall. The only change is the breakdown of liquidity between Central Banks and foreign banks to the advantage of the former. In parallel, as banks undertook significant efforts in summer to sell Lebanese Eurobonds out of their portfolio holdings to foreign institutional investors, their FC sovereign exposure fell to 13.24% of FC deposits and 83.22% of shareholders' equity.

At the profitability level, the year 2016 witnessed so far a 9.7% growth in Alpha banks net profits, reinforcing return ratios at large. The return on average assets rose from 1.00% in the first nine months of 2015 to 1.17% in the 2016 corresponding period, while the return on average equity rose from 11.33% to 13.05%. Despite the rise in cost of funding by 10 basis points between the two periods (mainly due to FC funding that rose from 3.51% to 3.64%), Alpha banks spread improved by 4 bps to reach 1.94% as a result of the improving yield on earning assets combined with a growing share of average interest earning assets to average assets. The most significant development was at the level of non-interest income which rose from 0.88% of average assets in the first nine months of 2015 to 1.32% in the 2016 corresponding period, partly due to the non-recurrent BDL transactions, raising asset utilization from 2.78% to 3.26% between the two periods. At the current return ratios, Alpha banks are close to their average cost of equity, following the divergence reported in the past few years amid tough operating conditions in their main markets of presence.