Alpha Group Overview | Q3-2018

Sound financial standing in front of adverse operating conditions for Alpha banks

The Alpha Report, outlining the performance and positioning of the first 15 banks in Lebanon with deposits exceeding US$ 2 billion, was issued by Bankdata Financial Services for the first nine months of 2018.

Measured by the consolidated assets of Alpha banks, their banking activity continued to report positive growth. Assets grew by 7.0% over the first nine months of 2018, to move from US$ 232.8 billion in December 2017 to US$ 249.2 billion in September 2018, mainly driven by BDL financial engineering operations. While foreign activity contracted by 8.4% over the 9-month period amid exchange rate translation effects, domestic activity rose by 9.9% over the said period.

At the funding level, the Alpha banks domestic deposit growth since the beginning of the year registered a moderate level of US$ 3.6 billion (the equivalent of 2.3%), less than the US$ 6.9 billion growth reported over the same period of last year and less than the average growth of US$ 5.4 billion reported over the same period of the past five years.

This year's 9-month period also saw net domestic conversions from Lebanese Pounds to foreign currencies amid overall political uncertainties. Since the beginning of the year, total deposit growth is driven to the extent of 72% in foreign currency and 28% in Lebanese Pound. This has raised domestic deposit dollarization slightly further to 67.7% in September 2018.

On the lending side, the year 2018 reported the first contraction in a couple of decades. Loans to the domestic private sector contracted by US$ 1.1 billion over the first nine months of 2018, while they rose by US$ 1.7 billion over the 2017 same period and by an average of US$ 1.2 billion over the same period of the past five years. The breakdown by currency suggests that domestic FX loans contracted by US$ 1.2 billion, while LP loans rose by US$ 0.1 billion over the nine-month period.

Domestic interest rate hikes in the banking sector translated into a yearly increase in the average cost of LP funds for Alpha banks by 43 basis points between the first 9 months of 2017 and the same period in 2018, in addition to a yearly increase in the average FX cost of funds by 24 bps, below the rise in the US benchmark rate, the 3-month Libor, by 107 bps between September 2017 and September 2018. Corrollarily, the spread between LP and FX cost of funds rose from from 1.22% in September 2017 to 1.40% in September 2018.

Despite cost control efforts on behalf of Alpha banks, the overall tough operating conditions, as reflected by the net contraction in lending portfolios so far this year and the adverse effects of domestic tax hikes, lead to a 13.8% contraction in net profits (-9.7% for domestic net profits). As such, Alpha banks posted declining profitability ratios, with an annualized return on assets ratio of 0.94% against 1.17% over the same period last year, and an annualized return on equity ratio of 10.48% (11.43% for return on common equity), against 12.65% (14.01% for return on common equity) over the same period last year.

The components of return ratios suggest that asset utilization declined noticeably from 2.90% to 2.48% over the same 9-month periods, driven mainly by the decrease in non-interest income to average assets from 1.02% to 0.55%, while interest margins increased from 1.95% to 2.03%. The net operating margin likewise declined in parallel from 40.45% to 37.94%, driven by an increase in cost to income ratio from 46.27% to 48.35%, a rise in credit cost from 4.98% to 5.44% and an increase in tax cost from 8.03% to 8.21% between the two periods.

While there is no doubt that operating conditions became increasingly tougher for Lebanese banks in general and Alpha banks in particular, the strong financial standing of these banks put them in a firm position to withstand pressures emanating from the atypical operating environment surrounding them, be it in Lebanon or in their respective markets of presence.