Punjab National Bank | **INR: 1,271**

Reduce

Introduction

Punjab National Bank (PNB) is the second largest PSU bank in India in terms of business size. Bank has a 100% subsidiary PNB Investment Services Ltd. exclusively for Merchant Banking activities. has international presence in 9 countries, with a branch at Kabul, 2 branches in Hong Kong, representative offices at Almaty, Dubai, Shanghai and Oslo, a wholly owned subsidiary in UK (with 5 branches), and a joint venture with Everest Bank Ltd. Nepal. Currently, bank has ~4,951 branches and ~57,000 employees. Bank is set to acquire 64% stake in JSC Dana Bank, Kazakhstan for $24 million by 2010 will help it expand its operations in central Asia and Russia. Further, bank is in the process of setting up of representative offices (RO) in Sydney and upgrading its RO in Norway to a full fledge branch and setting up a wholly owned subsidiary in Canada, head quartered at Vancouver.

Key Investment Rationale

Expect above industry average growth in FY11

In Q1FY11 bank's advances grew by 24.6% y-o-y driven by SME and large corporate segments. Going forward too the growth will come predominantly from these two segments. Advances grew by 25.7% CAGR over FY06-10. We expect bank's credit growth to be above than the industry average and have modeled in a 22.5% CAGR over FY10-12.

Stable margins at ~2.8% - During Q1FY11, the Net Interest Margin (NIM) of the bank remained stable at 3.94%, highest amongst the PSU banks. We expect margins to remain buoyant at 3.5% despite pressure on account of rise in deposit rates and sluggish credit demand in Q2FY11E.

Profitability more immune from volatile bond yields

Bank's non-interest income is less dependent on the volatile treasury gains as its AFS portfolio is one of the lowest in the industry at 18.2% while AFS duration is 2.35 years. We don't expect that bond yields volatility will have any significant impact on bank's profitability in near future. Moreover, we have considered lower treasury gains for the FY11 and FY12.

Asset quality manageable

The Gross NPA of the bank grew by 12.4% sequentially to Rs 3,614 crore in QFY11 however it shot up by 38.6% on y-o-y basis. The delinquencies rose sharply during the quarter at 0.6% (2.4% annualized) as Rs1,216 crore of assets (including Rs 263.8 crore) from the restructured asset portfolio) slipped during the quarter. Bank's provision coverage ratio, including the technical write offs, stood at 77.6% much above the mandated 70% which provides enough cushion for any negative surprise on slippages side.

We have estimated slippages for the FY11 at around Rs 3200 crore which is 1.4% of the advances against 1.52% in FY10. Further, the size of the restructure book was 6.6% of the advances and out of that 8% turned NPA till June 2010 quarter. We believe Gross NPA at 1.82% and Net NPA at 0.66% are manageable for the bank.

Valuations & Views

Currently stock is trading at 1.63x P/ABV on FY12E ABV of Rs 780. We expect that the earnings will grow by 20.6% CAGR over FY10-12E against 36.3% CAGR over FY07-10. ROAE and ROAA will remain robust at 23% and 1.4% respectively in the next two fiscals.

However, we believe that most of the positive things have already been priced in and thus there is limited upside potential. We recommend investors to use the current rally driven by overseas portfolio investments to prune their exposure to the stock. Further, we would be buying the stock at 1,100 levels.

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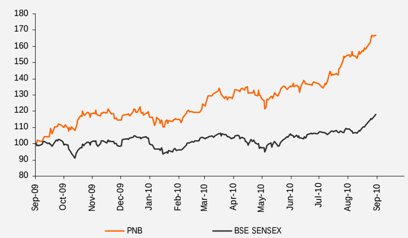
Price Target (INR): 1,342

Market Data	Sep 21, 2010
Shares outs (Cr)	31.5
Equity Cap (Rs. Cr)	315.0
Mkt Cap (Rs. Cr)	61,663
52 Wk H/L (Rs)	1,326/757
Avg Vol (1yr avg)	68,741
Face Value (Rs)	10



Market Info:

SENSEX	20001
NIFTY	6009

Share Holding pattern (%)

Particulars	Jun10	Mar10	Chg
Promoters	57.8	57.8	0
Institutions	18.2	18.3	-0.1%
FIIs	19.1	19.1	0.0%
Public & Others	4.9	4.8	0.1%
Total	**100.0**	**100.0**	

Source: BSE

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