

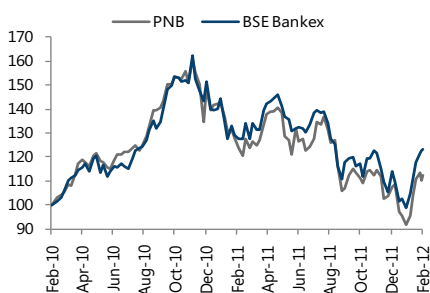
Q3FY12 - Result Update

Sell

Reco	Maintained
CMP	₹ 963
Target Price	₹ 900
Downside Potential	6.5%

Price Performance

52 wk Hi/Lo	1235/753
All time Hi/Lo	1400/35
6 mnth Average Vol	387587
Stock Beta	0.82



Valuation

	FY11	FY12P	FY13P
P/E (x)	6.7	6.2	5.3
P/BV (x)	1.5	1.2	1.0
P/ABV (x)	1.7	1.4	1.1
RONW (%)	24.4	21.8	21.6

Peer Valuation (FY12)

	SBI	BOB	Avg
PE	8.7	6.2	4.9
P/BV (x)	1.8	1.4	1.0

Equity Data

Market Cap. (₹ bln)	305
Face value (₹)	10
No of shares o/s (mln)	317

	Dec'10	Dec'11	Δ%
Promoters	57.80	58.00	0.35
DFI's	17.70	17.85	0.85
FII's	19.42	18.61	-4.17
Public	5.08	5.54	9.05

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Punjab National Bank

Asset quality deterioration amplifies

Punjab National Bank's (PNB) numbers came below our expectation both on core income and earnings front as NII grew by 10.4% y-o-y while Net profit grew by 5.5% as against our expectation of 13.4% and 19.4% growth respectively. The key reasons for the variance were i) decline in q-o-q margins by 7bps and ii) higher than expected provisions. While the concerns on asset quality already existed, the extent of deterioration is a shocker with further weakening in the offering.

Business growth healthy

The business of the bank grew by 21.4% y-o-y with Advances and Deposits growing by 18.7% and 23.4% y-o-y respectively. Domestic Advance growth was fairly stable at 15.6% increase with broad based growth coming from Retail (+19.7%), SME (+18.5%) and Corporate (15.5%). However the Overseas growth was very strong at 83% y-o-y growth. Deposits were driven by Term Deposits which were up by 31% while CASA ratio declined by 95bps q-o-q to 35.3%.

Core Income growth lower as margins shrink q-o-q

The NII growth of the bank was 10.4% as margins for the bank declined by 7bps to 3.88% due to sequential increase in Cost of deposits by 22bps while Yield on advances growth was just 5bps. For FY12, management has guided NIM at 3.5% levels.

Slippages higher than anticipated

While we had built in the stress on the asset quality, the magnitude of slippages for the quarter was a shocker with Gross and Net NPA's increasing by 25% & 39% respectively q-o-q on absolute basis. Slippage ratio increased to 2.6% as against 1.6% q-o-q with recoveries and upgradations too were lower than the previous quarter run rate. The restructured book increased by ₹ 19.84bln of which ₹ 10bln pertains to telecom sector. This book now forms 6.4% of the loan book. While the bank has not restructured any SEB loans this quarter, discussions are on with Rajasthan SEB though that would not entail any NPV hit. However given the current stressed asset book, dropping coverage levels (70% incl w/offers vs 75% q-o-q) and further likely bloating of restructured book, we remain cautious on the asset quality.

Valuation

The profitability of the bank is under pressure since past few quarters given the higher credit costs and with further slippages and incremental restructuring expected, provisions are likely to remain higher thus straining the earnings. We have marginally tweaked our FY12E estimates to factor in higher provisions. The stock currently trades at 1.4x & 1.1x of its FY12E & FY13E ABV respectively. While the valuations appear reasonable we remain cautious on the asset quality of the bank and hence maintain our "Sell" with a target price of ₹ 900.

Summary Financials

₹ in Mln	FY10	FY11	FY12P	FY13P
Net Interest Income	85229	118073	135509	158568
Other Income	34125	36126	42460	44416
Pre-Provisioning Profit	73263	90557	106828	121929
Net Profit	39053	44335	47821	56653
EPS	123.9	139.9	150.9	178.8
Networth	177229	215086	253954	299339
Deposits	2493298	3128987	3754785	4543290
Advances	1866012	2421067	2905280	3457283

Exhibit 1: Q3FY12 Performance Highlights

Punjab National Bank

Particulars (₹ in mln)	Q3FY12	Q3FY11	(y-o-y)	(q-o-q)	9MFY12	9MFY11	(y-o-y)
Interest Income	94,810	71,191	33.2	5.9	267,483	195,462	36.8
Interest Expense	59,444	39,158	51.8	8.1	166,438	107,679	54.6
Net Interest Income (NII)	35,366	32,033	10.4	2.4	101,045	87,987	14.8
Other Income	9,541	8,572	11.3	7.3	29,266	24,672	18.6
Net Total Income	44,907	40,605	10.6	3.4	130,311	112,457	15.9
Operating Expenses	18,143	17,106	6.1	0	53,530	46,974	14
Pre-Provisioning Profit (PPP)	26,764	23,499	13.9	5.9	76,781	65,483	17.3
Provisions & Contingencies	9,461	7,139	32.5	33.2	25,499	17,641	44.6
PBT	17,303	16,360	5.8	-4.8	51,282	47,843	7.2
Tax	5,803	5,463	6.2	-5.2	16,681	15,515	7.5
PAT	11,500	10,898	5.5	-4.6	34,601	32,328	7
EPS	36.3	34.6	5	-4.6	145.6	136.7	6.5
Cost to Income (%)	40.4	42.1	-172.7	-137.5	41.1	41.8	-0.7
GNPA (%)	2.4	2.0	0.4	0.4	2.4	2	0.4
NNPA (%)	1.1	0.7	0.4	0.3	1.1	0.7	0.4

Key Q3FY12 Result Highlights

Business growth healthy

The business of the bank grew by 21.4% y-o-y with Advances and Deposits growing by 18.7% and 23.4% y-o-y respectively. Deposits were driven by Term Deposits which were up by 31% while CASA ratio declined by 95bps q-o-q to 35.3%. C-D ratio stood at 74.58% as against 77.45% y-o-y.

Exhibit 2: Trend in Business growth

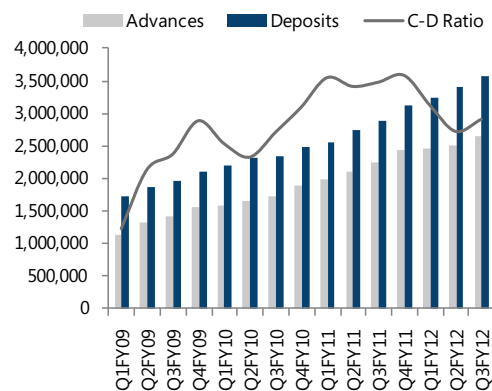
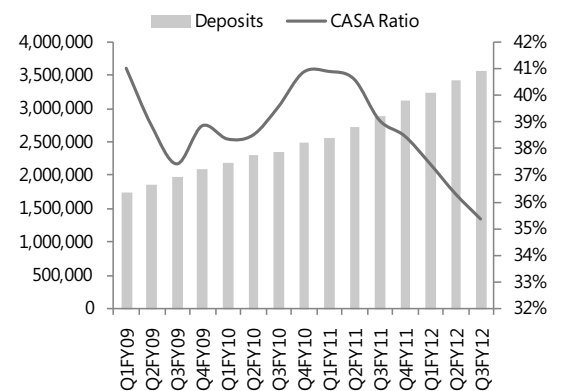


Exhibit 3: Trend in CASA ratio



Source: Company, MSFL Research

Advance grew by 18.7% y-o-y of which Overseas Advances grew strongly by 83% y-o-y due to low base while growth in Domestic Advances was rather subdued with 15.6% y-o-y; more in-line with the industry trend. Growth in Domestic Advances was broad based coming from Retail (+19.7%), SME (+18.5%) and Corporate (15.5%).

Exhibit 4: Break up of Advances

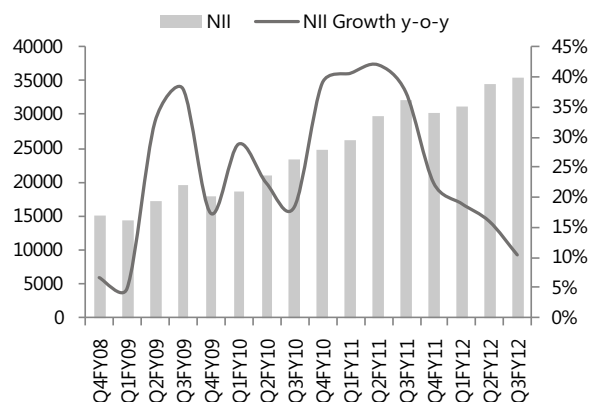
Particulars	Q3FY12	Q3FY11	% y-o-y	Q2FY12	q-o-q
Gross Advances	2658840	2237440	18.8%	2517050	5.6%
International	197780	108170	82.8%	165110	19.8%
Domestic Advances	2461060	2129270	15.6%	2351940	4.6%
Retail	260090	217320	19.7%	247320	5.2%
SME	299120	252490	18.5%	276430	8.2%
Corporate	884120	765450	15.5%	907600	-2.6%
Agri & Allied	383060	339090	13.0%	350760	9.2%
Services & Other	476600	412780	15.5%	424150	12.4%

Source: Company, MSFL Research

Core Income lower than expected

The NII growth of the bank was 10.4% as against our expectations of 13.4% growth as margins for the bank declined by 7bps to 3.88% q-o-q as well as contraction in C-D ratio.

Exhibit 5: Trend in NII growth



Source: Company, MSFL Research

Margins decline in contrast of industry trend

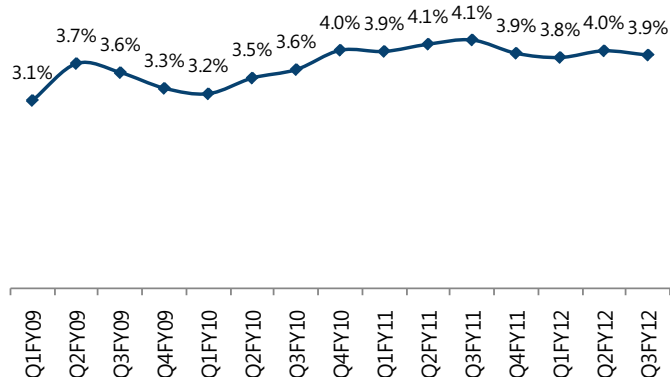
The NIM of the bank declined by 7bps q-o-q; in contrast of industry trend where most of the banks witnessed sequential improvement in margins. The decline is due to sequential increase in Cost of deposits by 22bps while Yield on advances grew by just 5bps. For FY12, management has guided NIM at 3.5% levels.

Exhibit 6: Spread Analysis (Reported)

(in %)	Q3FY12	Q3FY11	chg y-o-y	chg q-o-q
Yield on advances	11.97%	10.59%	138.00	5.00
Yield on investments	7.86%	6.82%	104.00	8.00
Yield on Funds	9.18%	8.25%	93.00	17.00
Cost of deposits	6.74%	5.20%	154.00	22.00
Cost of funds	5.76%	4.54%	122.00	22.00

Source: Company, MSFL Research

Exhibit 7: Trend in NIM movement (Reported)



Source: Company, MSFL Research

Other Income growth fairly stable

The fee based income of the bank grew strongly by 26.9% y-o-y while the growth in exchange profits was by 23%. However the treasury income of the bank was flattish y-o-y while the recoveries were lower by 25% leading to overall other income growth of 11.3%.

Exhibit 8: Break up of Other Income

Particulars	Q3FY12	Q3FY11	% y-o-y	Q2FY12	q-o-q
CEB	5100	4020	26.9%	5790	-11.9%
Treasury	870	870	0.0%	530	64.2%
Forex	1540	1250	23.2%	1330	15.8%
Dividend Income MF	80	170	-52.9%	520	-84.6%
Recovery	920	1230	-25.2%	800	15.0%
Other Income	1031	1032	-0.1%	-81	-
Total	9541	8572	11.3%	8889	7.3%

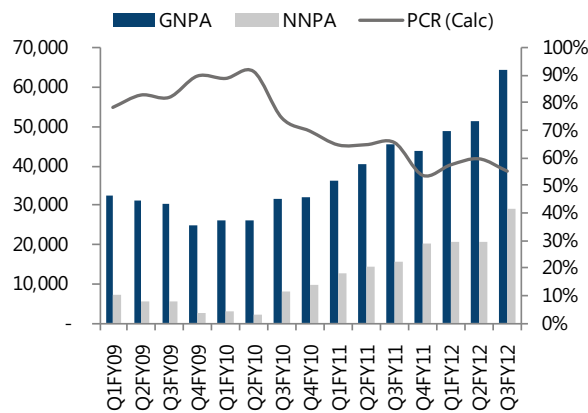
Source: Company, MSFL Research

Slippages higher than anticipated

While we had built in the stress on the asset quality, the magnitude of slippages for the quarter was a shocker with Gross and Net NPA's increasing by 25% & 39% respectively q-o-q on absolute basis. Slippage ratio increased to 2.6% as against 1.6% q-o-q with recoveries and upgradations too were lower than the previous quarter run rate. The Gross and Net NPA ratio stood at 2.42% and 1.11% respectively as against 2.05% and 0.84% in the previous quarter. Despite of increase in the credit costs, the PCR fell to 55% on calculated basis while including write-offs it was at 70% vs 75% in the previous quarter.

The restructured book increased by ₹ 19.84bln of which ₹ 10bln pertains to telecom sector. This book now forms 6.4% of the loan book. While the bank has not restructured any SEB loans this quarter, discussions are on with Rajasthan SEB though that would not entail any NPV hit. However given the current stressed asset book, dropping coverage levels (70% incl w/offs vs 75% q-o-q) and further likely bloating of the restructured book, we remain cautious on the asset quality.

Exhibit 9: Trend in Asset Quality



Source: Company, MSFL Research

Other Highlights

- The Capital Adequacy Ratio (CAR) of the bank stood at 11.48% with Tier-I capital at 7.85% and Tier-II ratio at 3.36%. Including 9MFY12 profits, the CAR would have been at 12.79%. Bank is expecting ₹ 12.85bln of capital infusion from the government by FY12 which would further enhance its Tier-I capital.
- Cost to Income ratio stood at 41.4% as against 41.8% in the previous quarter.

Outlook and Valuation

The profitability of the bank is under pressure since past few quarters given the higher credit costs and with further slippages and incremental restructuring expected, provisions are likely to remain higher thus straining the earnings. We have marginally tweaked our FY12E estimates to factor in higher provisions. The stock currently trades at 1.4x & 1.1x of its FY12E & FY13E ABV respectively. While the valuations appear reasonable we remain cautious on the asset quality of the bank and hence maintain our Sell with a target price of ₹ 900.

Financial Summary

Profit & Loss

Particulars (₹ in mln)	2009	2010	2011	2012P	2013P
Interest Income	191,272	214,669	269,865	352,677	435,176
Interest Expense	122,953	129,440	151,791	217,168	276,608
Net Interest Income (NII)	68,319	85,229	118,073	135,509	158,568
Other Income	30,647	34,125	36,126	42,460	44,416
Total Net Income	98,966	119,354	154,199	177,969	202,984
Operating Expenses	42,062	46,091	63,642	71,141	81,056
Pre-Provisioning Profit (PPP)	56,904	73,263	90,557	106,828	121,929
Provisions & Contingencies	9,235	14,215	24,920	35,454	37,372
PBT	47,669	59,048	65,637	71,374	84,557
Tax	16,760	19,994	21,302	23,554	27,904
PAT	30909	39053	44335	47821	56653
NIM (Calculated)	3.1%	3.1%	3.5%	3.3%	3.2%
EPS	98.0	123.9	139.9	150.9	178.8
NII Growth (%)	23.4%	24.8%	38.5%	14.8%	17.0%
PAT Growth (%)	50.9%	26.4%	13.5%	7.9%	18.5%

Balance Sheet

Particulars (₹ in mln)	2009	2010	2011	2012P	2013P
Liabilities					
Equity	3,153	3,153	3,168	3,168	3,168
Reserves & Surplus	143,383	174,076	211,917	250,786	296,171
Networth	146,536	177,229	215,086	253,954	299,339
Deposits	2,097,605	2,493,298	3,128,987	3,754,785	4,543,290
Borrowings	124,597	192,624	315,897	301,093	316,147
Other Liabilities & Provisions	100,448	103,177	123,283	206,513	248,942
Total Liabilities	2,469,186	2,966,328	3,783,252	4,516,345	5,407,718
Assets					
Cash & balances with RBI	170,583	183,276	237,769	256,845	334,310
Balances with banks & money at call	43,549	51,460	59,143	79,163	99,577
Investments	633,852	777,245	951,623	1,163,983	1,408,420
Advances	1,547,030	1,866,012	2,421,067	2,905,280	3,457,283
Fixed Assets	23,971	25,135	31,056	32,609	33,587
Other Assets	50,202	63,201	82,594	78,464	74,541
Total Assets	2,469,186	2,966,328	3,783,252	4,516,345	5,407,718

Ratios

Valuation Ratios	2009	2010	2011	2012P	2013P
P/E	9.6	7.6	6.7	6.2	5.3
P/BV	2.3	1.8	1.5	1.2	1.0
P/ABV	2.3	1.9	1.7	1.4	1.1
P/PPP	5.3	4.1	3.4	2.9	2.5
EPS	98.0	123.9	139.9	150.9	178.8
DPS	20.0	22.0	22.0	24.3	30.5
Book Value (BV)	416.7	514.8	632.5	755.2	898.4
Adjusted Book Value (ABV)	408.4	483.6	568.1	686.5	823.5

Profitability Ratios

ROE	25.8%	26.6%	24.4%	21.8%	21.6%
ROA	1.4%	1.4%	1.3%	1.2%	1.1%

Spread Analysis

	2009	2010	2011	2012P	2013P
Yield on Advances	10.6%	9.8%	9.8%	10.5%	10.8%
Yield on Investments	7.3%	6.5%	6.5%	6.7%	6.8%
Cost of Deposits	6.1%	5.2%	4.9%	5.9%	6.3%
Cost of Funds	6.0%	5.1%	4.8%	5.6%	6.0%
Net Interest Margin (NIM)	3.1%	3.1%	3.5%	3.3%	3.2%

Key Assumptions

Credit Growth	-	-	-	20.0%	19.0%
Deposit Growth	-	-	-	20.0%	21.0%
CASA Ratio	-	-	-	40.0%	41.0%
Slippage Ratio	-	-	-	2.0%	1.8%
Provisioning coverage	-	-	-	65.2%	67.8%

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Key ratings:

Rating	Expected Return
Buy	> 15%
Accumulate	5 to 15%
Hold	-5 to 5%
Sell	< -5%
Not Rated	-

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