

Punjab National Bank

Rs1,115

OUTPERFORMER

RESULT NOTE

Mkt Cap: Rs354.8bn; US\$7.8bn

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Result: Q3FY11

Comments: Robust performance

Revision: Reducing FY11 estimates by 6% and FY12 estimates by 3%

Key valuation metrics

Year to March 31 (Rs m)	NII	yoy chg (%)	Net profit	yoy chg (%)	EPS (Rs)	Adj. Book value Rs/share	P/Adj.Bk (x)	PER (x)	RoE (%)
FY08	55,342	6.2	20,488	10.6	65	350	3.2	17.3	19.6
FY09	70,309	27.0	30,909	50.9	98	435	2.6	11.5	25.8
FY10	85,229	21.2	39,054	26.4	124	518	2.2	9.1	26.5
FY11E	121,999	43.1	45,373	16.2	144	632	1.8	7.8	25.0
FY12E	147,387	20.8	58,019	27.9	184	785	1.4	6.1	26.0

Key highlights

Punjab National Bank (PNB) reported a net profit of Rs10.9bn, below our estimate of Rs11.6bn. The underperformance was due to elevated provision expenses and higher operating expenditure. However, NII remained strong on the back of a sequential expansion in margins and robust loan growth.

- **Strong NII growth; margin uptrend continues:** NII came in at ~Rs32bn (ahead of our estimate of Rs31.1bn), a strong 45% yoy growth, buoyed by ~7bp qoq expansion in NIMs and robust business volumes. Reported NIMs stood at 4.13%, with a rise in cost of funds offset by a rise in yield on advances and investments. PNB also received an income tax refund of Rs1.1bn during the quarter. (Exhibit 1)
- **Robust loan growth:** PNB's loan book grew by a strong 30% yoy and ~6% qoq to Rs2213bn, led by 13% qoq growth in retail advances (33% yoy) and 9% qoq growth in SME advances. The management is targeting loan growth of 25% in FY11 and above industry 22-25% in FY12. (Exhibit 4)
- **High slippages...:** Gross NPAs increased by ~Rs5.2bn qoq to Rs45.4bn (at 2.03%, a 12bp qoq rise). Slippages came in at Rs9.8bn – annualized 1.9% of opening advances. However, the management indicated that ~Rs6bn of slippages emanated from five large chunky accounts, which are expected to get upgraded in the coming quarters. As a result, higher recoveries and up-gradations are expected to restrict credit costs. (Exhibit 5)
- **...lead to higher than expected provisions:** NPA provisions came in higher than our estimates at Rs7.1bn. Of these, NPA provisions amounted to Rs5.6bn (a 55% qoq rise). PNB also made standard assets provisioning of Rs1.1bn during the quarter. Coverage ratio (including technical write-offs) was stable sequentially at 77.2%. (Exhibit 6)
- **Higher opex:** Operating expenses rose by 38% yoy to Rs17.1bn, ahead of our estimates. The bank made Rs2.4bn of second pension provisions and Rs1.3bn of gratuity provisions in Q3FY11. The management indicated that the total second option pension provision liability is expected to be ~Rs36bn. Assuming an amortization period of five years; the bank would have to make Rs7.2bn of pension provisions each year. Other operating expenses rose by 19% yoy to Rs4.9bn in Q3FY11.

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- **Healthy CASA ratio:** While total deposits increased by 6% qoq, CASA deposits increased by 2% qoq. So the CASA ratio declined by 154bp qoq to 39.1%, but remains one of the best in the industry. The proportion of bulk deposits increased to 22.4% (20.3% in Q2FY11). (Exhibit 2)
- **Traction in non-fund income:** Overall non-interest income grew by a strong 19% qoq (stable yoy on a high base) to Rs8.6bn. Non-trading income too displayed traction with 13% yoy growth. Core fee income (CEB plus forex) witnessed 23% yoy growth to Rs6.2bn in Q2FY11. (Exhibit 3)
- **Capital adequacy:** CAR came in at 11.9%, with a tier I ratio of 7.6% in Q3FY11. Including YTD profits, Tier I ratio would stand increased to ~9% in Q3FY11.

Valuations and view

PNB delivered a robust performance as NIMs were sustained and loan growth continued to be strong. Fee income was healthy due to traction in core fee and forex income. Though slippages and provisions were higher than expected, the management expects higher up-gradations and recoveries to restrict increase in gross NPAs in the future. We see concerns on PNB's asset quality abating as buoyant economic growth and an elevated coverage ratio (77%) are likely to limit provisioning expenses. With sustained NII momentum, led by a superior margin profile and strong loan growth, we see PNB on track to deliver continued earnings. On account of higher-than-expected provisions, we have lowered our FY11 and FY12 earnings estimates by 6% and 3% respectively. With a 22% CAGR in earnings over FY10-12E and an average RoE of 25%, current valuations of 1.4x FY12E P/BV appear attractive. We reiterate Outperformer with a 12-month price target of Rs1490 (1.9x FY12E adj. BV).

Quarterly results

(Rs m)	Q3FY10	Q4FY10	Q1FY11	Q2FY11	Q3FY11	FY10	FY11E	FY12E
Total intt income	53,887	56,076	59,919	64,554	71,191	214,669	282,032	355,127
Interest expense	31,764	31,097	33,733	34,787	39,158	129,440	160,032	207,740
Net interest income	22,123	24,980	26,186	29,767	32,033	85,229	121,999	147,387
<i>yoy growth (%)</i>	12.4	31.0	45.4	42.1	44.8	21.2	43.1	20.8
Other income	8,478	8,532	8,715	7,183	8,572	34,125	32,707	36,329
<i>yoy growth (%)</i>	(10.3)	(0.3)	(15.5)	7.4	1.1	16.9	(4.2)	11.1
Trading gains	1,570	1,380	1,210	380	870	8,030	3,300	3,000
Non trading income	4,870	4,630	5,910	5,050	6,220	26,095	29,407	33,329
Net revenue	30,601	33,511	34,901	36,950	40,605	119,354	154,706	183,716
Operating expenses	12,419	11,001	13,919	15,949	17,106	47,619	64,286	79,518
Operating profit	18,182	22,510	20,982	21,001	23,499	71,735	90,421	104,198
<i>yoy growth (%)</i>	0.7	41.7	33.7	30.7	29.2	24.9	26.0	15.2
Total provisions	2,819	6,219	5,341	5,160	7,139	14,215	22,700	17,602
PBT	15,363	17,106	15,640	15,841	16,360	59,048	67,721	86,596
Tax	5,250	5,756	4,958	5,095	5,463	19,994	22,348	28,577
PAT	10,113	11,350	10,683	10,746	10,898	39,054	45,373	58,019
<i>yoy growth (%)</i>	0.5	31.1	28.4	15.9	7.8	26.4	16.2	27.9
Ratios (%)								
Net interest margin	3.2	3.5	3.5	3.7	3.8	3.1	3.7	3.6
Non fund rev/Avg assets	1.2	1.2	1.1	0.9	1.0	1.3	1.0	0.9
Core fee inc/Avg assets	0.7	0.6	0.8	0.6	0.7	0.6	0.6	0.6
Op expenses/avg assets	1.8	1.5	1.8	2.0	2.0	1.8	1.9	2.0
Tot prov/avg assets	0.4	0.9	0.7	0.6	0.8	0.5	0.7	0.4
PBT/avg assets	2.2	2.4	2.1	2.0	1.9	2.2	2.0	2.1
PAT/ avg assets	1.5	1.6	1.4	1.3	1.3	1.4	1.4	1.4
Tax/PBT	34.2	33.6	31.7	32.2	33.4	33.9	33.0	33.0
CRAR	14.6	14.2	13.8	12.6	11.9			
Tier- I CRAR	9.3	9.2	8.7	8.0	7.6			
CD Ratio	72.8	74.8	77.1	76.4	76.6			

Quarterly results

Balance Sheet (Rs bn)	Q3FY10	Q4FY10	Q1FY11	Q2FY11	Q3FY11	FY10	FY11E	FY12E
Credit	1,704	1,866	1,969	2,088	2,213	1,866	2,351	2,892
yoy change (%)	20.4	20.6	24.6	27.6	29.8	20.6	26.0	23.0
Deposits	2,339	2,493	2,553	2,734	2,889			
yoy change (%)	18.7	18.9	16.6	18.4	23.5			

* calculated on average quarterly assets

Exhibit 1: Strong NIM performance

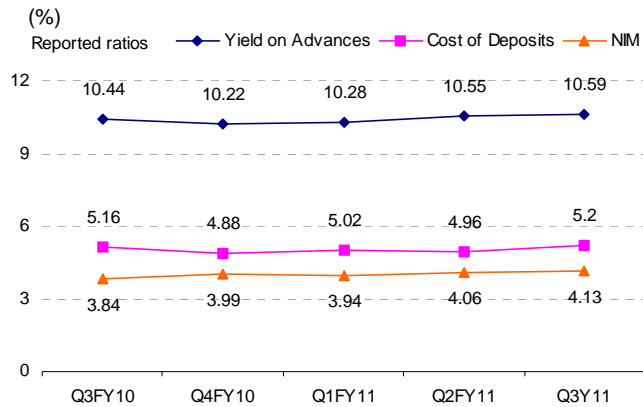


Exhibit 2: CASA declines

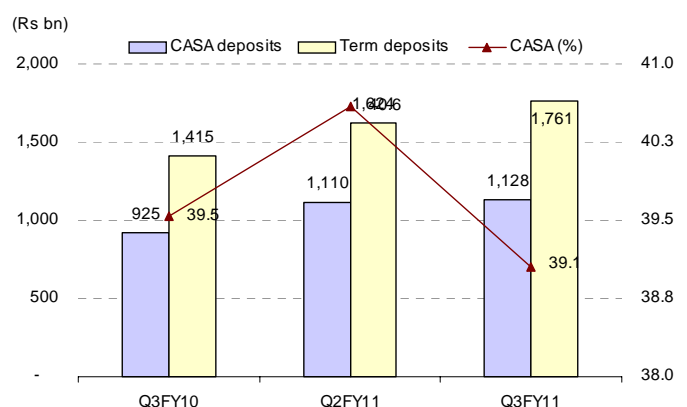


Exhibit 3: Non-interest income break up

Rs mn	Q3FY10	Q2FY11	Q3FY11	% yoy change	% qoq change
Forex	800	310	1,250	56.3	303.2
CEB	4,070	4,740	4,970	22.1	4.9
Fee income	4,870	5,050	6,220	27.7	23.2
Trading	1,570	380	870	(44.6)	128.9
Others	2,038	1,753	1,482	(27.3)	(15.4)
of which: Recoveries	770	890	1,230	59.7	38.2
Total	8,478	7,183	8,572	1.1	19.3

Exhibit 4: Composition of loan book (%)

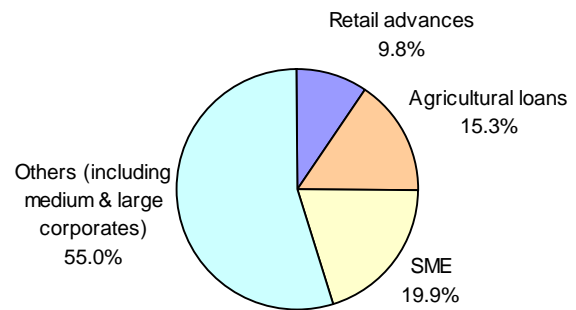


Exhibit 5: Gross NPAs inch-up

	Q3FY10	Q2FY11	Q3FY11	Incremental qoq (Rsm/bp)
Gross NPAs (Rs m)	31,556	40,248	45,411	5,163
Net NPAs (Rs m)	8,119	14,255	15,751	1,496
Gross NPA (%)	1.83	1.91	2.03	12bp
Net NPA (%)	0.48	0.69	0.72	3bp
Provision Coverage (%)	74.3	64.6	65.3	73bp
Restructured loans (Rs bn)				
Incremental	5.5	5.4	8.2	
Cumulative	105.9	135.4	143.6	
As a % of net loans	6.2	6.5	6.5	

Exhibit 6: NPA Provisions rise

	Q3FY10	Q2FY11	Q3FY11	% yoy change
Prov for NPA	3,290	3,590	5,550	68.7
Provision for depreciation	420	670	440	4.8
Other prov.	(141)	120	59	(141.7)
Total provisions	2,819	5,160	7,139	153.3
Standard asset/ restruct provisions	-750	780	1090	(245.3)

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