

October 28, 2010

Reco	Previous Reco
Buy	Buy
CMP	Target Price
Rs1,310	Rs1,500
EPS change FY11E/12E (%)	NA
Target Price change (%)	9.5
Nifty	5,998
Sensex	19,941

Price Performance

(%)	1M	3M	6M	12M
Absolute	1	23	27	54
Rel. to Nifty	1	11	12	24

Source: Bloomberg

Relative Price Chart



Source: Bloomberg

Stock Details

Sector	Banks
Bloomberg	PNB@IN
Equity Capital (Rs mn)	3153
Face Value(Rs)	10
No of shares o/s (mn)	315
52 Week H/L	1,360/819
Market Cap (Rs bn/USD mn)	413/9,279
Daily Avg Volume (No of sh)	322993
Daily Avg Turnover (US\$m)	8.9

Shareholding Pattern (%)

	S'10	J'10	M'10
Promoters	57.8	57.8	57.8
FII/NRI	19.5	19.1	19.1
Institutions	17.8	18.2	18.3
Private Corp	0.9	0.9	0.8
Public	3.9	4.0	4.0

Source: Capitaline

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- **PNB's Q2FY11 NII at Rs29.8bn better than expectations driven by 6% qoq growth in advances and 12bps expansion in NIMs. Net profit at Rs10.7bn in line with expectations**
- **Slippages surprise positively at Rs9.1bn lower than Rs12.1bn reported in Q1FY11. However, gross NPAs rise due to lower recoveries. Provision cover strong at 77% (RBI norms)**
- **Other positives in the result – (1) CASA at 40.6% despite strong growth in balance sheet (2) provisions done at 65% on net incremental slippages and (3) robust fee income growth**
- **Valuations not unreasonable at 2.2x FY11E/1.7x FY12E ABV. Continue BUY rating with TP of Rs1500**

Strong growth in NII...

PNB's NII for Q2FY11 has grown by 13.7% qoq to Rs29.8bn. The strong growth in NII was driven by 6% qoq growth in advances and 12bps expansion NIMs

... As NIMs expands qoq – positive surprise

We are positively surprised by 12bps qoq expansion in PNB's Q2FY11 NIMs as the NIMs are already the highest in the industry. The expansion in NIMs was driven by 30bps expansion in yield on advances and stable cost of deposits.

We expect the NIMs to come down in Q3FY11 as the bank has revised the deposit rates during Q2FY11, the effect of which will reflect in next quarter. For FY11, we have built in NIMs assumption of 3.5%.

Yield analysis

%	Q2FY10	Q3FY10	Q4FY10	Q1FY11	Q2FY11	YoY (bps)	QoQ (bps)
Yield on advances*	10.3	10.0	9.7	9.8	9.9	-40	14
Yield on investments*	6.4	7.1	6.5	6.4	6.7	24	25
Yield on assets*	8.3	8.0	7.8	7.9	8.1	-18	19
Cost of funds*	5.2	4.6	4.3	4.4	4.4	-81	-9
NIM*	3.1	3.4	3.5	3.5	3.7	62	28
Yield on Fund#	8.2	8.2	7.8	8.0	8.2	-1	15
Cost of Fund#	5.1	4.7	4.4	4.5	4.4	-72	-11
NIMs#	3.5	3.8	4.0	3.9	4.1	56	12

Source: Company, Emkay Research

Note:* Calculated on basis of average quarterly balances

reported, reported NIMs on earning assets

Valuation table

Y/E March 31	Net income	Net profit	EPS (Rs)	ABV (Rs)	RoA (%)	RoE (%)	PE (x)	P/ABV (x)
FY2009	99,506	30,909	98.0	408.4	1.4	22.9	13.3	3.2
FY2010	120,882	39,054	123.9	475.1	1.4	24.1	10.5	2.7
FY2011E	145,882	44,948	142.6	600.0	1.4	23.0	9.1	2.2
FY2012E	172,498	56,548	179.3	767.7	1.4	23.9	7.2	1.7

Source: Company, Emkay Research

Key financials – Quarterly

Rs mn	Q2FY10	Q3FY10	Q4FY10	Q1FY11	Q2FY11	YoY (%)	QoQ (%)	YTD' 11	YTD' 10	YoY (%)
Net Interest Income	19,922	23,291	24,980	26,189	29,767	49.4	13.7	55,956	38,540	45.2
Other Income	7,713	7,310	8,532	8,715	7,183	-6.9	-17.6	15,897	17,415	-8.7
Fee Income	3,810	3,820	3,950	4,960	4,740	24.4	-4.4	9,700	8,399	15.5
Net Income	27,636	30,602	33,511	34,904	36,950	33.7	5.9	71,853	55,956	28.4
Total Operating Expenses	11,573	12,419	11,001	13,919	15,949	37.8	14.6	29,868	24,199	23.4
<i>As % Of Net Income</i>	<i>41.9</i>	<i>40.6</i>	<i>32.8</i>	<i>39.9</i>	<i>43.2</i>			<i>41.6</i>	<i>43.2</i>	
Employee Expenses	7,276	8,327	6,532	9,952	11,131	53.0	11.8	21,083	16,352	28.9
<i>As % Of Net Income</i>	<i>26.3</i>	<i>27.2</i>	<i>19.5</i>	<i>28.5</i>	<i>30.1</i>			<i>29.3</i>	<i>29.2</i>	
Other Expenses	4,297	4,092	4,469	3,967	4,818	12.1	21.4	8,785	7,847	12.0
<i>As % Of Net Income</i>	<i>15.5</i>	<i>13.4</i>	<i>13.3</i>	<i>11.4</i>	<i>13.0</i>			<i>12.2</i>	<i>14.0</i>	
Operating Profit	16,063	18,182	22,510	20,984	21,001	30.7	0.1	41,986	31,757	32.2
<i>As % Of Net Income</i>	<i>58.1</i>	<i>59.4</i>	<i>67.2</i>	<i>60.1</i>	<i>56.8</i>			<i>58.4</i>	<i>56.8</i>	
Provisions	2,163	2,820	6,216	5,341	5,160	138.5	-3.4	10,501	5,183	102.6
Prov for NPA	565	3,290	4,620	5,500	3,590	535.5	-34.7	9,090	2,035	346.7
PBT	13,900	15,362	17,109	15,643	15,841	14.0	1.3	31,484	26,574	18.5
Total Tax	4,634	5,250	5,756	4,958	5,095	10.0	2.8	10,053	9,267	8.5
Adjusted PAT	9,266	10,112	10,813	10,686	10,746	16.0	0.6	21,432	17,306	23.8
Extra Ordinary Items	0	0	0	0	0					
Reported PAT	9,266	10,112	10,813	10,686	10,746	16.0	0.6	21,432	17,306	23.8
Reported EPS	29.4	32.1	36.0	33.9	34.1	16.0	0.6	68.0	54.9	23.8

Source: Company, Emkay Research

Retail and SME segment witness strong growth

PNB's advances for the quarter have grown by 6.0% qoq as the retail and SME segment witnessed strong growth. Amongst industries, textiles, cement and roads segment reported strong growth. However, we remain wary of the fact that the growth in large corporate lagging behind SME, will raise the risk in the portfolio in long term.

Advances mix

Rs bn	Q2FY10	Q3FY10	Q4FY10	Q1FY11	Q2FY11	YoY (%)	QoQ (%)
Retail	170	179	191	194	226	32.7	16.2
Agriculture	250	272	302	302	323	29.0	6.7
SME	244	327	350	370	403	65.4	8.8
Others	972	927	1,022	1,102	1,136	16.9	3.1
Total	1,636	1,704	1,866	1,969	2,088	27.6	6.0

Source: Company, Emkay Research

CASA remains stable despite high growth

The CASA remained stable at 40.6% in Q2FY11 despite higher growth in advances. The growth was driven by strong growth of ~6.3% qoq in CASA balances.

CASA Mix

Rs bn	Q2FY10	Q3FY10	Q4FY10	Q1FY11	Q2FY11	YoY (%)	QoQ (%)
Savings Deposits	191	199	237	225	237	24.3	5.1
Current Deposits	698	726	781	818	873	25.1	6.7
CASA	888	925	1,019	1,044	1,110	24.9	6.3
Term deposits	1,420	1,415	1,475	1,510	1,624	14.4	7.6
Total Deposits	2,308	2,339	2,493	2,553	2,734	18.4	7.1
Demand/Total	38.5	39.5	40.8	40.9	40.6	211	-29

Source: Company, Emkay Research

Fee income growth reflects strong balance sheet growth

The fee income reflected the growth in balance sheet as the income from streams like LC/processing fees showed sharp 35%+ yoy growth. As expected the trading gains were significantly lower.

Other income

Rs mn	Q2FY10	Q3FY10	Q4FY10	Q1FY11	Q2FY11	YoY (%)	QoQ (%)	YTD' 11	YTD' 10	YoY (%)
Fee/Commission income	3,810	3,820	3,950	4,960	4,740	24.4	-4.4	9,700	8,399	15.5
Trading gains/(losses)	2,531	1,570	1,380	1,215	380	-85.0	-68.7	1,595	6,116	-73.9
Forex gains/(losses)	550	750	1,220	950	310	-43.6	-67.4	1,260	1,160	8.6
Dividend income	350	770	1,400	760	890	154.3	17.1	1,650	990	66.7
Other non int income	472	400	581	830	863	82.7	3.9	1,693	751	125.5
Total	7,713	7,310	8,532	8,715	7,183	-6.9	-17.6	15,897	17,415	-8.7

Source: Company, Emkay Research

Fee income

Rs mn	Q2FY10	Q3FY10	Q4FY10	Q1FY11	Q2FY11	YoY (%)	QoQ (%)	YTD' 11	YTD' 10	YoY (%)
Bills	330	370	350	280	330	0.0	17.9	610	660	-7.6
LC/LG	1,020	1,320	1,340	1,310	1,400	37.3	6.9	2,710	2,080	30.3
Locker Rent	110	120	130	120	130	18.2	8.3	250	230	8.7
Processing Fees	1,090	1,150	1,530	2,100	1,480	35.8	-29.5	3,580	3,110	15.1
Others	1,260	860	600	1,150	1,400	11.1	21.7	2,550	2,320	9.9
Exchange	550	750	1,220	950	310	-43.6	-67.4	1,260	1,160	8.6
Total	4,360	4,570	5,170	5,910	5,050	15.8	-14.6	10,960	9,560	14.6

Source: Company, Emkay Research

Core operating profit grows 4% qoq

As the bank provided Rs2.5bn for employee related provisions, the Opex grew by 14.6% qoq. The staff expenses were also higher due to the revision in DA expenses during the quarter. However, adjusted for provisions and trading gains, the core operating profit has grown by 53.8% yoy or 4% qoq.

While we believe that there is a possibility that the actual pension liabilities may turn out be more or less than the provisions being done now, the same can be compensated as PNB wouldn't have to do the gratuity provisions (Rs1.25bn/quarter) from next year onwards.

Core operating profit

Rs mn	Q2FY10	Q3FY10	Q4FY10	Q1FY11	Q2FY11	YoY (%)	QoQ (%)	YTD' 11	YTD' 10	YoY (%)
Reported operating profit	16,063	18,182	22,510	20,984	21,001	30.7	0.1	41,986	31,757	32.2
Less: Treasury gains	2,531	1,570	1,380	1,215	380	-85.0	-68.7	1,595	6,116	-73.9
Employee related provisions	1,500	250	1,000	2,500	2,500	66.7	0.0	5,000	4,000	25.0
Core operating profit	15,032	16,862	22,130	22,270	23,121	53.8	3.8	45,391	29,641	53.1

Source: Company, Emkay Research

Provisions come down with slippages

The provisions for NPAs dropped by about a third in line with lower slippages incurred during the quarter. However, we are comforted by the fact that the provisioning costs has been kept high during H1FY11 at 0.8% (annualised) thereby using strong profits to strengthen the balance sheet.

Break up of provisions

Rs mn	Q2FY10	Q3FY10	Q4FY10	Q1FY11	Q2FY11	YoY (%)	QoQ (%)	YTD' 11	YTD' 10	YoY (%)
On NPL	565	3,290	4,620	5,500	3,590	535.5	-34.7	9,090	2,035	346.7
As % of advances	0.03	0.19	0.25	0.28	0.17			0.44	0.12	
On Standard Assets	740	-750	498	171	780	5.4	356.1	951	2,000	-52.5
Investment Depreciation	828	420	-60	140	650	-21.5	364.3	790	328	140.6
Others	30	-140	1,158	-470	140	367.7	-129.9	-330	820	-140.2
Total	2,163	2,820	6,216	5,341	5,160	138.5	-3.4	10,501	5,183	102.6

Source: Company, Emkay Research

Slippages slow down – lower than our expectations

The slippages dipped by ~25% qoq to Rs9.1bn at 0.4% (1.6% annualized). However, due to much lower recoveries, the gross NPAs have moved up by ~Rs4bn. The provision cover including the technical write offs, was at 77%. We have built slippages of Rs39bn or 1.6% pf advances for FY11.

NPA profile

Rs bn	Q2FY10	Q3FY10	Q4FY10	Q1FY11	Q2FY11	YoY (%)	QoQ (%)
Gross NPA (Rs bn)	26,186	31,556	32,144	36,138	40,248	53.7	11.4
Net NPA (Rs bn)	2,327	8,119	9,817	12,833	14,255	512.7	11.1
Gross NPA (%)	1.6	1.8	1.7	1.8	1.9		
Net NPA (%)	0.1	0.5	0.5	0.7	0.7		
Net NPLs/Net worth (%)	1.4	4.7	5.5	6.8	7.2		
Provision cover (%)	91.1	74.3	69.5	64.5	64.6		

Source: Company, Emkay Research

Slippages

Rs mn	Q2FY10	Q3FY10	Q4FY10	Q1FY11	Q2FY11	YoY (%)	QoQ (%)
Cumulative (Rs mn)	8,590	19,850	28,380	12,160	21,270	147.6	
Quarterly (Rs mn)	3,250	11,260	8,530	12,160	9,110	180.3	-25.1
Cumulative (%)	0.5	1.2	1.5	0.6	1.0		
Quarterly (%)	0.2	0.7	0.5	0.6	0.4		

Source: Company, Emkay Research

Capital adequacy remains comfortable

The capital adequacy remained comfortable during the quarter with tier I CAR at 9.06% (including profit of H1FY11). The total CAR (including H1FY11 profit) stood at 13.6%.

Valuations and view

The stock is currently quoting at 2.2x FY11E ABV and 1.7x FY11E ABV with attractive RoEs of 23.5%. We do not find the valuations unreasonable looking at strong returns profile. We have already factored in slippage rate of 160bps and provision cost of 90bps in our numbers. We maintain our BUY rating on the stock with price target of Rs1500 (2x FY12E ABV).

Key Financials

Income Statement (Rs. Mn)

(Year Ending Mar 31)	FY09	FY10	FY11E	FY12E
Net interest income	70,309	85,229	112,375	134,319
Other income	29,197	35,653	33,507	38,179
Net income	99,506	120,882	145,882	172,498
Operating expenses	42,062	47,619	54,951	59,847
Pre provision profit	57,443	73,263	90,931	112,651
PPP excl treasury	64,090	81,296	95,931	117,651
Provisions	9,809	14,237	22,995	27,184
Profit before tax	47,634	59,026	67,935	85,467
Tax	16,725	19,973	22,987	28,919
Tax rate	35%	34%	34%	34%
Profit after tax	30,909	39,054	44,948	56,548

Balance Sheet (Rs. Mn)

(Year Ending Mar 31)	FY09	FY10	FY11E	FY12E
Liabilities				
Equity	3,153	3,153	3,153	3,153
Reserves	143,383	174,076	210,171	257,127
Net worth	146,536	177,229	213,324	260,280
Deposits	2,097,605	2,493,298	3,080,314	3,631,511
Borrowings	225,255	296,052	347,105	403,946
Total liabilities	2,469,396	2,966,579	3,640,742	4,295,737
Assets				
Cash and bank	214,131	234,736	280,234	330,379
Investments	589,148	746,918	903,396	1,050,326
Customer assets	1,591,734	1,896,339	2,362,839	2,817,031
Others	74,383	88,587	94,274	98,002
Total assets	2,469,396	2,966,579	3,640,742	4,295,737

Key Ratios (%)

(Year Ending Mar 31)	FY09	FY10	FY11E	FY12E
NIM	3.2	3.2	3.5	3.5
Non-Il/avg assets	1.3	1.3	1.0	1.0
Fee income/avg assets	0.6	0.6	0.6	0.6
Opex/avg assets	1.9	1.8	1.7	1.5
Provisions/avg assets	0.5	0.5	0.9	0.9
PBT/avg assets	1.9	2.0	1.9	2.0
Tax/avg assets	0.7	0.7	0.6	0.7
RoA	1.4	1.4	1.4	1.4
RoAE	22.9	24.1	23.0	23.9
GNPA (%)	2.0	1.9	1.7	1.5
NNPA (%)	0.2	0.7	0.4	0.1

Valuations Table

(Year Ending Mar 31)	FY09	FY10	FY11E	FY12E
Net profit (Rs mn)	30,909	39,054	44,948	56,548
Shares in issue (mn)	315	315	315	315
EPS (Rs)	98.0	123.9	142.6	179.3
PER (x)	13.3	10.5	9.1	7.2
FDEPS(Rs)	98.0	123.9	142.6	179.3
FDPER (x)	13.3	10.5	9.1	7.2
Book value (Rs)	416.7	514.8	629.3	778.2
P/BV (x)	3.1	2.5	2.1	1.7
Adj book value (Rs)	408.4	475.1	600.0	767.7
P/ABV (x)	3.2	2.7	2.2	1.7
P/PPP (x)	7.1	5.6	4.5	3.6
Dividend yield (%)	1.5	1.7	1.8	2.0

Recommendation History: Punjab National Bank – PNB IN

Date	Reports	Reco	CMP	Target
22/07/2010	Punjab National Bank Q1FY11 Result Update	Accumulate	1,056	1,100
07/05/2010	Punjab National Bank Q4FY10 Result Update	Accumulate	1,044	1,100
28/01/2010	Punjab National Bank Q3FY10 Result Update	Accumulate	860	950
30/10/2009	Punjab National Bank Q2FY10 Result Update	Hold	840	770

Recent Research Reports

Date	Reports	Reco	CMP	Target
27/10/2010	Union Bank of India Q2FY11 Result Update	Hold	393	400
26/10/2010	United Bank of India Q2FY11 Result Update	Hold	141	150
22/10/2010	Bank of India Q2FY11 Result Update	Reduce	537	450
22/10/2010	Corporation Bank Q2FY11 Result Update	Buy	735	860

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