

January 21, 2011

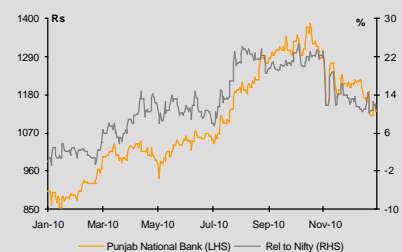
Reco	Previous Reco
Buy	Buy
CMP	Target Price
Rs1,123	Rs1,500
EPS change FY11E/12E (%)	NA
Target Price change (%)	NA
Nifty	5,697
Sensex	19,008

Price Performance

(%)	1M	3M	6M	12M
Absolute	(6)	(15)	7	24
Rel. to Nifty	(2)	(9)	2	11

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	1,591/692
Market Cap (Rs bn/USD mn)	354/7,602
Daily Avg Volume (No of sh)	31961
Daily Avg Turnover (US\$m)	1.0

Shareholding Pattern (%)

	D'10	S'10	J'10
Promoters	57.8	57.8	57.8
FII/NRI	19.5	19.5	19.1
Institutions	17.7	17.8	18.2
Private Corp	1.1	0.9	0.9
Public	4.0	3.9	4.0

Source: Capitaline

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- **PNB's Q3FY11 NII at Rs32bn in line with estimates driven by 6% qoq growth in advances and 7bps expansion in NIMs. PAT at Rs10.9bn lower than expected due to higher provisions**
- **NPAs inch up as the recoveries remain moderate during the quarter. Slippages remain in line with Q2FY11 at Rs9.7bn for the quarter. Provision cover strong at 77.8% (RBI norms)**
- **Other positives in the result – (1) CASA at 39.1% despite strong growth in balance sheet (2) provisions at 71% of net new slippages and (3) accelerated provisions for pension**
- **PAT growth lower this year on higher provisions. To bounce back as (1) staff provisions and (2) slippages come done in FY12E Valuations reasonable at 2.0x FY11E/1.6x FY12E ABV**

Strong growth in NII...

PNB's NII for Q3FY11 has grown by 37% yoy to Rs32.0bn. Even adjusted for one-off items, the growth is strong at 32% yoy and 4% qoq. The strong growth in NII was driven by 6% qoq growth in advances and 7bps expansion NIMs.

... As NIMs expands qoq/stable adjusted for one-off items

PNB's NIMs have expanded by 7bps qoq during the quarter even as the cost of funds has gone up by 15bps. However, adjusted for one-off items the NIMs would have remained flat. However, PNB has revised its BPLR/Base rate by 75/100bps which will help raise the yield on advances in coming quarters and help sustain margins. However, we are already building in NIM compression of 20bps in FY12E

Yield analysis

%	Q3FY10	Q4FY10	Q1FY11	Q2FY11	Q3FY11	YoY (bps)	QoQ (bps)
Yield on advances*	10.0	9.7	9.8	9.9	10.2	17	28
Yield on investments*	7.1	6.5	6.4	6.7	6.8	-27	16
Yield on assets*	8.0	7.8	7.9	8.1	8.5	44	39
Cost of funds*	4.6	4.3	4.4	4.4	4.7	2	30
NIM*	3.4	3.5	3.5	3.7	3.8	41	8
Yield on Fund#	8.2	7.8	8.0	8.2	8.3	6	10
Yield on advances#	10.4	10.2	10.3	10.6	10.6	15	4
Cost of Fund#	4.7	4.4	4.5	4.4	4.5	-19	15
NIMs#	3.8	4.0	3.9	4.1	4.1	29	7

Source: Company, Emkay Research Note:* Calculated on basis of average quarterly balances # reported

Profit growth moderates due to higher provisions

PNB's PAT for Q3FY11 has grown by 13% yoy (28% in Q1FY11 and 16% in Q2FY11) driven by higher provisions on pension and on NPAs. We believe the growth to bounce back to 20% in FY12E as employee provisions moderate and slippages come down.

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	11.7	2.8
FY2010	120,882	39,054	123.9	475.1	1.4	24.1	9.2	2.4
FY2011E	151,607	44,091	139.8	578.4	1.3	22.6	8.2	2.0
FY2012E	177,487	55,472	175.9	736.9	1.4	23.6	6.5	1.6

Source: Company, Emkay Research

Key financials – Quarterly

Rs mn	Q3FY10	Q4FY10	Q1FY11	Q2FY11	Q3FY11	YoY (%)	QoQ (%)	YTD' 11	YTD' 10	YoY (%)
Net Interest Income	23,291	24,980	26,189	29,767	32,041	37.6	7.6	87,997	61,832	42.3
Other Income	6,600	8,532	8,715	7,183	8,573	29.9	19.4	24,470	24,016	1.9
Net Income	29,892	33,511	34,904	36,950	40,614	35.9	9.9	112,468	85,847	31.0
Total Operating Expenses	12,419	11,001	13,919	15,949	17,106	37.7	7.3	46,974	36,618	28.3
As % Of Net Income	41.5	32.8	39.9	43.2	42.1			41.8	42.7	
Employee Expenses	8,327	6,532	9,952	11,131	12,235	46.9	9.9	33,319	24,680	35.0
As % Of Net Income	27.9	19.5	28.5	30.1	30.1			29.6	28.7	
Other Expenses	4,092	4,469	3,967	4,818	4,871	19.0	1.1	13,655	11,939	14.4
As % Of Net Income	13.7	13.3	11.4	13.0	12.0			12.1	13.9	
Operating Profit	17,472	22,510	20,984	21,001	23,508	34.5	11.9	65,494	49,229	33.0
As % Of Net Income	58.5	67.2	60.1	56.8	57.9			58.2	57.3	
Provisions	2,820	6,216	5,341	5,160	7,140	153.2	38.4	17,641	8,003	120.4
PBT	15,362	17,109	15,643	15,841	16,368	6.5	3.3	47,852	41,936	14.1
Total Tax	5,250	5,756	4,958	5,095	5,463	4.0	7.2	15,515	14,517	6.9
Adjusted PAT	9,645	10,813	10,686	10,746	10,906	13.1	1.5	32,337	26,951	20.0
Extra Ordinary Items	710	815	0	0	0			0	710	
Reported PAT	10,112	11,353	10,686	10,746	10,906	7.8	1.5	32,337	27,419	17.9
Reported EPS	32.1	36.0	33.9	34.1	34.6	7.8	1.5	102.6	87.0	17.9

Source: Company, Emkay Research

Large/SME corporate segment drives advances growth

PNB's advances for the quarter have grown by 6.0% qoq as driven by the growth in large and SME corporate segment which grew in almost double digits. Amongst the industries, infrastructure (15.3% qoq), cement (8.7% qoq) and basic metals (5.7% qoq) witnessed strong growth.

Advances mix

Rs bn	Q3FY10	Q4FY10	Q1FY11	Q2FY11	Q3FY11	YoY (%)	QoQ (%)
Retail	179	191	194	217	192	7.5	-11.6
Agriculture	272	302	302	323	302	11.0	-6.4
SME	327	350	370	403	441	35.1	9.6
Others	927	1,022	1,102	1,145	1,277	37.8	11.5
Total	1,704	1,866	1,969	2,088	2,213	29.8	6.0

Source: Company, Emkay Research

Savings deposits grow despite having raised rates

Driven by faster balance sheet growth the CASA has dipped to 39.1%. Notably, the savings deposits have still grown by ~3% qoq despite PNB having raised its term deposit rates twice during H2CY10.

CASA Mix

Rs bn	Q3FY10	Q4FY10	Q1FY11	Q2FY11	Q3FY11	YoY (%)	QoQ (%)
Current Deposits	199	237	225	237	229	15.5	-3.1
Savings Deposits	726	781	818	873	899	23.7	2.9
CASA	925	1,019	1,044	1,110	1,128	22.0	1.6
Term deposits	1,415	1,475	1,510	1,624	1,761	24.5	8.4
Total Deposits	2,339	2,493	2,553	2,734	2,889	23.5	5.7
Demand/Total	39.5	40.8	40.9	40.6	39.1	-49	-154

Source: Company, Emkay Research

Fee income growth moderates due to lower processing fees

The fee income for the quarter grew by a moderate 3.1% yoy and 16.9% driven by lumpiness in the processing fees as they declined by almost 30% qoq. **However, including the other non-interest income (excluding trading and dividends), the growth would have been 30% yoy.**

Other income

Rs mn	Q3FY10	Q4FY10	Q1FY11	Q2FY11	Q3FY11	YoY (%)	QoQ (%)	YTD' 11	YTD' 10	YoY (%)
Fee/Commission income	3,820	3,950	4,960	4,740	3,940	3.1	-16.9	13,640	12,219	11.6
Trading gains/(losses)	860	1,380	1,215	380	870	1.2	128.9	2,465	6,976	-64.7
Forex gains/(losses)	750	1,220	950	310	1,250	66.7	303.2	2,510	1,910	31.4
Dividend income	770	1,400	760	890	1,230	59.7	38.2	2,880	1,760	63.6
Other non int income	400	581	830	863	1,283	220.6	48.7	2,975	1,151	158.6
Total	6,600	8,532	8,715	7,183	8,573	29.9	19.4	24,470	24,016	1.9

Source: Company, Emkay Research

Accelerates pension provisions; core operating profit grows 13.5% qoq

PNB has accelerated its pension provisions to Rs2.4bn/quarter while continuing gratuity provisions at Rs1.25bn/quarter. As a result, the Opex has grown by 12% qoq. However, adjusted for provisions and trading gains, the core operating profit has grown by 44.9% yoy or 13.5% qoq.

The total pension liability has been estimated at Rs36bn which will be adjusted over period of next five years. Hence, from Q1FY12 onwards the liabilities on pension per quarter will be ~Rs1.8bn only. PNB is likely to provide gratuity liability in totality by this year only. Thus, from Q1FY12, the provisions for pension/gratuity will be at Rs1.8bn/quarter compared with Rs2.5-3.6bn/quarter for this year.

Strong core operating profit

Rs mn	Q3FY10	Q4FY10	Q1FY11	Q2FY11	Q3FY11	YoY (%)	QoQ (%)	YTD' 11	YTD' 10	YoY (%)
Reported operating profit	17,472	22,510	20,984	21,001	23,508	34.5	11.9	65,494	49,229	33.0
Less: Treasury gains	860	1,380	1,215	380	870	1.2	128.9	2,465	6,976	-64.7
Employee related provisions	1,500	250	1,000	2,500	3,600	140.0	44.0	7,100	6,500	9.2
Core operating profit	18,112	21,380	20,770	23,121	26,238	44.9	13.5	70,129	48,753	43.8

Source: Company, Emkay Research

Provisions remain high as recoveries remain moderate

PNB has done provisions on the net incremental slippages at rate of 71%, up from ~45% for H1FY11. This has resulted in steep rise in provisions for NPAs by ~70% over last year.

Break up of provisions

Rs mn	Q3FY10	Q4FY10	Q1FY11	Q2FY11	Q3FY11	YoY (%)	QoQ (%)	YTD' 11	YTD' 10	YoY (%)
On NPL	3,290	4,620	5,500	3,590	5,550	68.7	54.6	14,640	5,325	174.9
As % of advances	0.19	0.25	0.28	0.17	0.25			0.66	0.31	
On Standard Assets	-750	498	171	780	1,090	NA	39.7	2,041	1,250	63.3
Investment Depreciation	420	-60	140	650	440	4.8	-32.3	1,230	748	64.4
Others	-140	1,158	-470	140	60	NA	-57.2	-270	680	NA
Total	2,820	6,216	5,341	5,160	7,140	153.2	38.4	17,641	8,003	120.4

Source: Company, Emkay Research

Slippages in line with previous quarter

The slippages during the quarter at Rs9.8bn were in line with previous quarter. However, due to much lower recoveries, the gross NPAs have moved up by ~Rs5bn. The provision cover including the technical write offs, was at 77%.

NPA profile

Rs bn	Q3FY10	Q4FY10	Q1FY11	Q2FY11	Q3FY11	YoY (%)	QoQ (%)
Gross NPA (Rs bn)	31,556	32,144	36,138	40,248	45,411	43.9	12.8
Net NPA (Rs bn)	8,119	9,817	12,833	14,255	15,751	94.0	10.5
Gross NPA (%)	1.8	1.7	1.8	1.9	2.0		
Net NPA (%)	0.5	0.5	0.7	0.7	0.7		
Net NPLs/Net worth (%)	4.7	5.5	6.8	7.2	7.5		
Provision cover (%)	74.3	69.5	64.5	64.6	65.3		

Source: Company, Emkay Research

Slippages

Rs mn	Q2FY10	Q3FY10	Q4FY10	Q1FY11	Q2FY11	YoY (%)	QoQ (%)
Cumulative (Rs mn)	19,850	28,380	12,160	21,270	31,040	56.4	
Quarterly (Rs mn)	11,260	8,530	12,160	9,110	9,770	-13.2	7.2
Cumulative (%)	1.2	1.5	0.6	1.0	1.4		
Quarterly (%)	0.7	0.5	0.6	0.4	0.4		

Source: Company, Emkay Research

Capital adequacy remains comfortable

The capital adequacy remained comfortable during the quarter with tier I CAR at 8.99% (including profit of M9FY11). The total CAR (including M9FY11 profit) stood at 13.3%.

Valuations and view

The need for higher provisions on all fronts like NPAs, gratuity and pension has resulted in just 13.1% yoy growth in PNB's profit for Q3FY11. The growth in profit after tax has consistently come down from 28% in Q1FY11 to 16% in Q2FY11 and to 13.1% now in Q3FY11.

We assuming the PAT growth in FY12 to bounce back to 20% driven by two things (1) the provisions for pension/gratuity are likely to come down by a third from Rs12.2bn in FY11 to Rs8.0bn in FY12 pension and (2) we have built in the slippages at 1.4% in FY12E compared with 1.7% this year.

The stock is currently quoting at 2.0x FY11E ABV and 1.6x FY11E ABV with attractive RoEs of 23.1%. We find the valuations reasonable looking at strong returns profile and on expectations of bounce back in profit growth in FY12E. We maintain our BUY rating on the stock with price target of Rs1500.

Key Financials**Income Statement (Rs. Mn)**

(Year Ending Mar 31)	FY09	FY10	FY11E	FY12E
Net interest income	70,309	85,229	118,416	139,558
Other income	29,197	35,653	33,190	37,929
Net income	99,506	120,882	151,607	177,487
Operating expenses	42,062	47,619	61,971	64,002
Pre provision profit	57,443	73,263	89,636	113,485
PPP excl treasury	64,090	81,296	92,936	116,785
Provisions	9,809	14,237	22,996	29,644
Profit before tax	47,634	59,026	66,640	83,841
Tax	16,725	19,973	22,549	28,369
<i>Tax rate</i>	35%	34%	34%	34%
Profit after tax	30,909	39,054	44,091	55,472

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	209,314	255,195
Net worth	146,536	177,229	212,467	258,348
Deposits	2,097,605	2,493,298	3,081,647	3,768,286
Borrowings	225,255	296,052	346,667	405,418
Total liabilities	2,469,396	2,966,579	3,640,781	4,432,051
Assets				
Cash and bank	214,131	234,736	280,355	342,822
Investments	589,148	746,918	903,751	1,086,785
Customer assets	1,591,734	1,896,339	2,362,839	2,903,183
Others	74,383	88,587	93,836	97,452
Total assets	2,469,396	2,966,579	3,640,781	4,432,051

Key Ratios (%)

(Year Ending Mar 31)	FY09	FY10	FY11E	FY12E
NIM	3.2	3.2	3.7	3.5
Non-Il/avg assets	1.3	1.3	1.0	0.9
Fee income/avg assets	0.6	0.6	0.6	0.6
Opex/avg assets	1.9	1.8	1.9	1.6
Provisions/avg assets	0.5	0.5	0.9	1.0
PBT/avg assets	1.9	2.0	1.8	1.9
Tax/avg assets	0.7	0.7	0.6	0.6
RoA	1.4	1.4	1.3	1.4
RoAE	22.9	24.1	22.6	23.6
GNPA (%)	2.0	1.9	2.2	2.2
NNPA (%)	0.2	0.7	0.7	0.4

Valuations Table

(Year Ending Mar 31)	FY09	FY10	FY11E	FY12E
Net profit (Rs mn)	30,909	39,054	44,091	55,472
Shares in issue (mn)	315	315	315	315
EPS (Rs)	98.0	123.9	139.8	175.9
PER (x)	11.7	9.2	8.2	6.5
FDEPS(Rs)	98.0	123.9	139.8	175.9
FDPER (x)	11.7	9.2	8.2	6.5
Book value (Rs)	416.7	514.8	626.5	772.1
P/BV (x)	2.7	2.2	1.8	1.5
Adj book value (Rs)	408.4	475.1	578.4	736.9
P/ABV (x)	2.8	2.4	2.0	1.6
P/PPP (x)	6.3	4.9	4.0	3.2
Dividend yield (%)	1.7	1.9	2.1	2.3

Recommendation History: Punjab National Bank – PNB IN

Date	Reports	Reco	CMP	Target
28/10/2010	Punjab National Bank Q2FY11 Result Update	Buy	1,310	1,500
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

Recent Research Reports

Date	Reports	Reco	CMP	Target
20/01/2011	LIC Housing Finance Company Update	Buy	174	210
20/01/2011	Yes Bank Q3FY11 Result Update	Accumulate	273	300
20/01/2011	South Indian Bank Q3FY11 Result Update	Buy	22	30
19/01/2011	LIC Housing Finance Q3FY11 Result Update	UR	170	UR

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