

Punjab National Bank

1 August 2019

Reuters: PNB.BO; Bloomberg: PNB IN

Growth, not asset quality, remains the main issue

Punjab National Bank (PNB) reported 1QFY20 results with the key pointers being (1) Slippages remained under relative control with GNPA addition at Rs 54.12bn compared with an 8-quarter average of Rs 178.09bn over FY17-18 (2) Domestic margin was largely stable when adjusted for one-offs, inching lower 3 bps YoY to 2.36% and (3) Growth remained the major issue with global loan growth at 3.2% YoY and domestic loan growth at 7.3% YoY. (See *comprehensive analyst meet takeaways* on page 2 for *significant incremental colour*). Per se, on the key P&L items, PNB posted NII decline of 12% YoY at Rs41,414mn, PPOP decline of 17% YoY at Rs34,814mn and PAT was back in the black at Rs10,186mn versus a loss of Rs9,400mn in the corresponding quarter last year. We have revised our estimates for FY20/FY21 and retained Accumulate rating on PNB, revising our target price to Rs73 (from Rs92 earlier), valuing the stock at 0.6x standalone FY21E P/ABV and ascribing a value of Rs22 for subsidiaries.

Slippages remained under relative control with GNPA addition at Rs 54.12bn compared with an 8-quarter average of Rs 178.09bn over FY17-18: As a consequence, provisions were down 65% YoY to Rs 20.23bn, driving an RoE of 9.6% for the quarter. Management sounded confident regarding the amendments to the IBC ideated by the Union Government in terms of aiding pending resolutions of key IBC accounts. Key IBC accounts worth Rs 70bn are expected to be resolved in the near term. Management also clarified that their exposure to stressed corporates currently in the news is low. Exposure to large stressed HFC is ~Rs 10bn. Management also averred that, going forward, ageing provisions are not going to be a major concern. They pointed to the fact that, of the GNPA stock of Rs 773bn, NCLT accounts comprise Rs 425bn, on which the PCR stands at 88%.

Domestic margin was largely stable when adjusted for one-offs, inching lower 3 bps YoY to 2.36%: Last year, PNB benefited from the recovery of a large RBI NCLT List 1 steel account with an incremental interest income of Rs 8bn due to the same. Going forward, margin could be supported by (1) Retailisation of loan book and (2) Cost of funds control. Yield on advances, at 7.61%, was up 34 bps YoY after adjusting for one off last year. Cost of deposits, at 5.21%, was up lesser (than Yield on Advances) at 22bps YoY. CASA ratio remained at a reasonably good level of 42.8%, up 27 bps YoY. Total domestic deposits growth was 8.1% YoY with CASA growth being 8.7% YoY. CA deposits were up 18% YoY to Rs 410bn.

Growth remained the major issue with global loan growth at 3.2% YoY and domestic loan growth at 7.3% YoY: Capital constraint continued to be a major drag on growth with common equity tier 1 ratio at 6.21% at the beginning of the quarter and 6.35% at the end of it. Regulatory minimum common equity tier 1 ratio requirement, along with capital conservation buffer, is 8% by the end of March 2020. Management explained that, right now, there is no immediate plan to go to the Union Government for additional equity capital. The bank has taken an approval for a fresh equity capital raise of Rs 50bn from the capital markets. Domestic loan growth was driven by retail loan growth of 22% YoY to Rs 912bn, within which housing loans grew 30% YoY to Rs 545bn.

Valuation and outlook: We have revised our NII estimates by -3.0%/-5.2%, PPOP estimates by -1.6%/-4.7% and PAT estimates by -4.2%/-7.5% for FY20/FY21, respectively. We have retained Accumulate rating on PNB, revising our target price to Rs73 (from Rs92 earlier), valuing the stock at 0.6x standalone FY21E P/ABV and ascribing a value of Rs22 for subsidiaries.

ACCUMULATE

Sector: Banking

CMP: Rs68

Target Price: Rs73

Upside: 9%

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Key Data

Current Shares O/S (mn)	4,604.0
Mkt Cap (Rsbn/US\$bn)	310.8/4.5
52 Wk H / L (Rs)	100/58
Daily Vol. (3M NSE Avg.)	31,834,510

Price Performance (%)

	1 M	6 M	1 Yr
Punjab National Bank	(16.5)	(8.7)	(22.8)
Nifty Index	(7.5)	0.8	(3.2)

Source: Bloomberg

Y/E March (Rsmn)	1QFY20	1QFY19	4QFY19	YoY (%)	QoQ (%)
Interest income	130,864	131,132	128,357	(0.2)	2.0
Interest expenses	89,451	84,213	86,354	6.2	3.6
Net interest income	41,414	46,919	42,003	(11.7)	(1.4)
Domestic NIM (%)	2.36	2.90	2.45	-54 bps	-9 bps
Non-interest income	20,753	19,592	18,894	5.9	9.8
Total income	62,167	66,511	60,897	(6.5)	2.1
Staff costs	16,817	14,273	19,899	17.8	(15.5)
Other operating expenses	10,536	10,291	12,386	2.4	(14.9)
Total operating expenses	27,352	24,564	32,285	11.4	(15.3)
Cost-to-income (%)	44.0	36.9	53.0	707 bps	-902 bps
Pre-provisioning operating profit	34,814	41,947	28,612	(17.0)	21.7
Provisions	20,233	57,582	100,711	(64.9)	(79.9)
PBT	14,581	(15,635)	(72,099)	NA	NA
Tax	4,395	(6,235)	(24,603)	NA	NA
-effective tax rate	30.1	39.9	34.1	-974 bps	-398 bps
PAT	10,186	(9,400)	(47,496)	NA	NA
EPS (Rs)	2.21	(3.41)	(12.38)	NA	NA
BV (Rs)	92.3	132.3	89.5	(30.3)	3.1
Deposits	6,724,714	6,303,114	6,760,301	6.7	(0.5)
Advances	4,217,938	4,153,395	4,582,492	1.6	(8.0)

Source: Company, Nirmal Bang Institutional Equities Research

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Comprehensive Analyst Meet Takeaways

Asset Quality

- Last year, the bank had introduced CLPCs (centralized loan processing centres) on pilot basis. The bank, during the quarter, has rolled out more number of CLPCs across the country, as part of its strategy to improve the quality of existing assets as well as incremental underwriting.
- CLPCs are manned by specialist manpower with functions such as monitoring, sourcing and disbursal separated from each other, as opposed to being clubbed together earlier. This step is essentially to mitigate people risk, as stated that by the bank.
 - For example, sourcing is now done at the branch level whereas approval and monitoring is carried out at CLPCs.
 - Underwriting is conducted at levels as deemed appropriate by the bank.
- For retail loans of less than Rs 50 lacs, sourcing is done at the branch level. For sourcing MSME loans, the bank is increasingly focusing on the loan-in-59-minutes platform.
- The bank stated that it is in the process of developing algo-based underwriting process for retail loans, which is expected to help improve quality of underwriting and reduce people risk.
- The bank stated that it has a work force of 2,700 people working under the stressed asset management vertical.
- In terms of NPA reduction during the quarter, the bank was expecting resolutions worth Rs. 70 bn pertaining to 2-3 accounts which got delayed due to judicial processes. However, the bank expects these resolutions to come through in Q2FY20 or Q3FY20.
- There was a release in investment depreciation during the quarter due to favourable yield movements and another release of Rs. 3.52 bn worth of provisions created last quarter against unhedged forex exposures.
- The bank has allotted sufficient power at the branch level to carry out OTS (one-time settlement schemes) for stressed loans of <Rs. 5mn ticket size. There is another OTS scheme for accounts of size varying between Rs 5 mn – Rs 500mn.
- Provisions, on QoQ basis, are low since Q4FY19 provisions consisted of a large chunk towards ageing provisions.
- The bank acknowledged that there has been some slowdown in MSMEs due to various reasons, including asset quality stress.
- 80% of the portfolio is not less than investment grade.
- Exposure to a large stressed housing finance company is ~Rs. 10 bn.

Business and Loan Growth

- The bank stated that it has launched a portal for the MSME segment which focuses on loans of below Rs. 1 lac. The aim of this portal is to facilitate faster processing of such loans.
- Bank has given a guidance of 10% credit growth during FY20.
- In context of the total loan book, real estate exposure is not high for the bank.
- Increase in unsecured loans is mostly towards AAA rated PSU companies.
- The bank stated that it is shrinking its international business and will be focusing on domestic business going forward.

Operating Expenses

- The bank stated that it is working towards improving operational efficiency. This could also include reduction in absolute levels of opex.
- The bank stated that it has closed down 4-5 overseas offices.

Fee and Other Income

- Treasury profit during the quarter was Rs. 5.01 bn.

Capital Adequacy

- The bank said there is no immediate plan to go to the Government for further capital raise. In fact, it is looking to raise Rs. 50 bn through either rights issue or QIP, for which an enabling board resolution has been taken.
- The bank stated that PNB Housing Finance stake sale process has not been able to materialize due to regulatory hurdles. However, the bank will still continue to pursue monetization of its non-core financial and non-financial (old headquarters) assets. This would contribute towards capital.

Exhibit 1: Financial summary

Y/E March (Rsmn)	FY17	FY18	FY19	FY20E	FY21E
Net interest income	149,931	149,224	171,563	179,141	196,058
Pre-provisioning operating profit	145,651	102,942	129,952	148,216	161,807
PAT	13,248	(122,828)	(99,755)	24,396	42,364
EPS (Rs)	6.5	(55.4)	(21.7)	4.9	8.5
BV (Rs)	197.8	148.8	97.3	98.3	104.4
P/E (x)	10.5	(1.2)	(3.1)	13.8	7.9
P/BV (x)	0.3	0.5	0.7	0.7	0.6
Gross NPAs (%)	12.5	18.4	15.5	12.7	11.2
Net NPAs (%)	7.8	11.2	6.6	3.4	1.7
RoA (%)	0.2	(1.7)	(1.3)	0.3	0.5
RoE (%)	3.3	(29.5)	(23.2)	5.2	8.4

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 2: Actual performance versus our estimates

(Rsmn)	1QFY20	1QFY19	4QFY19	YoY (%)	QoQ (%)	4QFY19	Devi. (%)
Net interest income	41,414	46,919	42,003	(11.7)	(1.4)	44,010	(5.9)
Pre-provisioning operating profit	34,814	41,947	28,612	(17.0)	21.7	34,598	0.6
PAT	10,186	(9,400)	(47,496)	(208.4)	(121.4)	1,838	454.2

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 3: Change in our estimates

	Revised estimate		Earlier estimate		% Revision	
	FY20E	FY21E	FY20E	FY21E	FY20E	FY21E
Net interest income (Rsmn)	179,141	196,058	184,663	206,756	(3.0)	(5.2)
NIM (%)	2.43	2.44	2.50	2.50	-7 bps	-6 bps
Operating profit (Rsmn)	148,216	161,807	150,571	169,790	(1.6)	(4.7)
Profit after tax (Rsmn)	24,396	42,364	25,470	45,818	(4.2)	(7.5)

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 4: One-year forward P/BV



Source: Company, Nirmal Bang Institutional Equities Research

Financials

Exhibit 5: Income statement

Y/E March (Rsmn)	FY17	FY18	FY19	FY20E	FY21E
Interest income	472,760	479,958	513,103	535,510	582,018
Interest expenses	322,828	330,734	341,539	356,369	385,959
Net interest income	149,931	149,224	171,563	179,141	196,058
Fee income	62,917	56,217	62,664	61,955	67,555
Other income	26,597	32,592	11,110	28,807	31,881
Net revenues	239,445	238,033	245,337	269,904	295,495
Operating expenses	93,794	135,091	115,385	121,687	133,688
-Employee expenses	54,207	91,688	69,632	74,029	81,722
-Other expenses	39,587	43,403	45,753	47,658	51,965
Pre-provisioning operating profit	145,651	102,942	129,952	148,216	161,807
Provisions	125,536	298,693	283,410	113,365	100,410
-Loan loss provision	131,453	229,458	248,709	107,192	96,012
-Investment depreciation	4,867	20,272	16,410	6,173	4,397
-Other provisions	(10,784)	48,964	18,292	0	0
PBT	20,115	(195,751)	(153,458)	34,851	61,397
Tax	6,867	(72,923)	(53,703)	10,455	19,033
PAT	13,248	(122,828)	(99,755)	24,396	42,364

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 7: Balance sheet

Y/E March (Rsmn)	FY17	FY18	FY19	FY20E	FY21E
Equity capital	4,256	5,521	9,208	9,945	9,945
Reserves & surplus	416,720	405,222	438,663	478,702	509,085
Shareholders' funds	420,976	410,743	447,871	488,647	519,030
Deposits	6,217,040	6,422,262	6,760,301	7,200,221	7,794,112
-Current deposits	458,533	403,742	443,751	496,815	545,588
-Savings deposits	2,141,625	2,228,731	2,406,654	2,563,279	2,805,880
-Term deposit	3,616,882	3,789,789	3,909,897	4,140,127	4,442,644
Borrowings	407,633	608,507	393,259	498,320	691,050
Other liabilities	157,657	216,789	148,063	178,877	198,479
Total liabilities	7,203,305	7,658,301	7,749,495	8,366,064	9,202,671
Cash/Equivalent	883,316	954,620	752,880	890,836	979,920
Advances	4,194,931	4,337,347	4,582,492	4,949,091	5,444,001
Investments	1,867,254	2,003,060	2,021,282	2,094,013	2,303,414
Fixed assets	62,732	63,493	62,248	68,473	75,321
Other assets	195,071	299,781	330,591	363,651	400,016
Total assets	7,203,305	7,658,301	7,749,495	8,366,064	9,202,671

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 6: Key ratios

Y/E March	FY17	FY18	FY19	FY20E	FY21E
Growth (%)					
NII growth	(2.1)	(0.5)	15.0	4.4	9.4
Pre-provision profit growth	19.2	(29.3)	26.2	14.1	9.2
PAT growth	NA	NA	(18.8)	NA	73.7
Business (%)					
Deposit growth	12.4	3.3	5.3	6.5	8.2
Advance growth	1.7	3.4	5.7	8.0	10.0
Business growth	7.9	3.3	5.4	7.1	9.0
CD	67.5	67.5	67.8	68.7	69.8
CASA	41.8	41.0	42.2	42.5	43.0
Operating efficiency (%)					
Cost-to-income	39.2	56.8	47.0	45.1	45.2
Cost-to-assets	1.4	1.8	1.5	1.5	1.5
Productivity (Rsmn)					
Business per branch	1,500.9	1,540.8	1,622.9	1,732.2	1,880.7
Business per employee	140.9	143.7	160.2	171.5	186.2
Profit per branch	1.9	(17.6)	(14.3)	3.5	6.0
Profit per employee	0.2	(1.6)	(1.4)	0.3	0.6
Spread (%)					
Yield on advances	7.9	7.5	7.9	7.8	7.8
Yield on investments	7.3	7.2	7.0	7.1	7.1
Cost of deposits	5.1	4.8	4.9	4.8	4.8
Yield on assets	7.3	7.0	7.3	7.3	7.3
Cost of funds	4.9	4.7	4.7	4.7	4.7
NIMs	2.3	2.2	2.4	2.4	2.4
Capital adequacy (%)					
Tier I	8.9	7.1	7.5	8.4	7.8
Tier II	2.8	2.1	2.2	2.1	2.0
Total CAR	11.7	9.2	9.7	10.5	9.8
Asset quality (%)					
Gross NPAs	12.5	18.4	15.5	12.7	11.2
Net NPAs	7.8	11.2	6.6	3.4	1.7
Specific provision coverage	62.8	60.0	76.4	84.8	91.5
Slippage	5.4	10.4	4.5	2.8	2.5
Credit-cost	3.1	5.7	5.5	2.2	1.8
Return (%)					
RoE	3.3	(29.5)	(23.2)	5.2	8.4
RoA	0.2	(1.7)	(1.3)	0.3	0.5
RoRWA	0.3	(2.7)	(2.3)	0.6	0.9
Per share					
EPS	6.5	(55.4)	(21.7)	4.9	8.5
BV	197.8	148.8	97.3	98.3	104.4
ABV	44.2	(27.6)	32.0	64.2	85.7
Valuation (x)					
P/E	10.5	(1.2)	(3.1)	13.8	7.9
P/BV	0.3	0.5	0.7	0.7	0.6
P/ABV	1.5	(2.4)	2.1	1.1	0.8

Source: Company, Nirmal Bang Institutional Equities Research

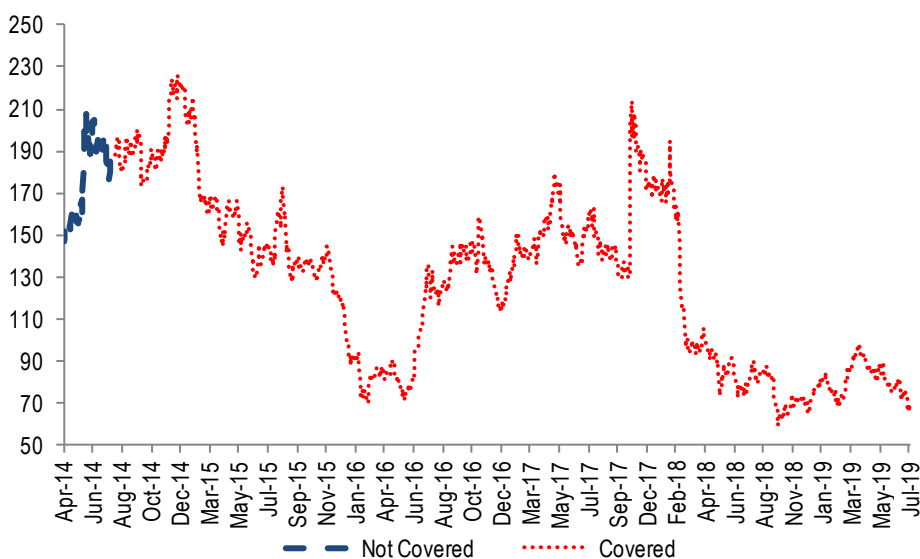
N.B. Although there might be asset sales in FY20, we are not factoring in the same to show normalized earnings and ROE.

Rating track

Date	Rating	Market price (Rs)	Target price (Rs)
28 July 2014	Accumulate	924	975
8 October 2014	Accumulate	878	975
22 October 2014	Accumulate	928	1,030
8 January 2015*	Accumulate	205	206
4 February 2015	Accumulate	177	200
11 May 2015	Accumulate	146	160
29 July 2015	Accumulate	143	160
10 February 2016	Sell	88	75
24 May 2016	Sell	72	55
1 August 2016	Sell	124	75
9 November 2016	Sell	141	92
9 February 2017	Sell	152	92
14 February 2017	Sell	142	100
22 May 2017	Sell	160	115
3 Aug 2017	Sell	158	110
8 November 2017	Under Review	191	-
7 February 2018	Under Review	161	-
16 May 2018	Under Review	84	-
9 August 2018	Under Review	80	-
19 September 2018	Accumulate	79	82
9 October 2018	Accumulate	63	67
5 November 2018	Accumulate	69	70
13 December 2018	Accumulate	71	73
6 February 2019	Accumulate	75	76
8 April 2019	Accumulate	93	95
30 May 2019	Accumulate	82	92
8 July 2019	Accumulate	82	92
1 August 2019	Accumulate	68	73

* Post stock split

Rating track graph



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BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

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