

Sector: Banks & Finance
Result Update

	Change
Reco: Hold	↔
CMP: Rs. 35	
Price Target: Rs. 40	↓
↑ Upgrade ↔ No change ↓ Downgrade	

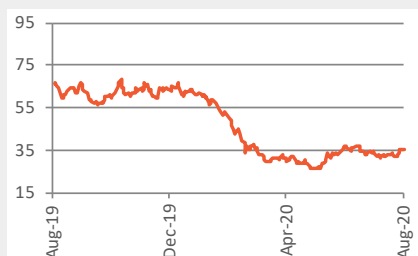
Company details

Market cap:	Rs. 33,219 cr
52-week high/low:	Rs. 69.6/26
NSE volume: (No of shares)	345.7 lakh
BSE code:	532461
NSE code:	PNB
Sharekhan code:	PNB
Free float: (No of shares)	135.7 cr

Shareholding (%)

Promoters	85.6
FII	1.1
DII	7.4
Others	5.9

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	5.2	32.2	-29.3	-46.3
Relative to Sensex	3.5	5.5	-25.6	-49.8

Sharekhan Research, Bloomberg

Punjab National Bank (PNB) posted largely in line with expectations results for Q1FY2021. Net interest income (NII) and PPOP came in line with expectations, but asset-quality performance was mixed. During the quarter, the bank had reported on amalgamated basis (erstwhile OBC and UBI merged in PNB) and, hence, prior-period reported performance is not strictly comparable. As of Q1FY2021, the bank had an elevated 29.2% (in value terms) of accounts under moratorium (which comprise borrowers who have missed two or more EMIs). The moratorium book has not declined on a sequential basis (most other peers have reported a decline) and, hence, is a dampener. On a restated comparable basis, amalgamated NII was flat on a sequential basis, but was up 8% y-o-y to Rs. 6,748 crore due to the decline in interest paid on borrowings. PPOP grew by 2.5% y-o-y to Rs. 5,280 crore, largely due to increased operating expense. Net profit for the quarter stood at Rs. 308 crore on account of lower provisions on a sequential basis. Provision for the quarter stood at Rs. 4,972 crore, lower sequentially, and NPA provisions declined to Rs. 4,836 crore sequentially. So far, the bank has made Rs. 1,027 crore COVID-19 provision, which we find to be relatively small compared to its book.

Asset-quality wise performance was mixed, with its gross NPA at 14.11% (up from 13.8% in Q4FY2020); however, NNPA improved marginally to 5.29% (down by 12 bps q-o-q). PCR improved sequentially to 80.75%, but NPA outlook continues to be weak, with pending provisions still an overhang. Due to the moratorium benefit, the quarter saw a sharp decline in slippage ratio to 1.51%, fall by 333 bps. Gross slippages were low at 1.4% but credit costs remained elevated at 3.2%. Net interest margin was stable at 2.47%, as lower cost of funds offset higher liquidity (loan-deposit ratio). CASA ratio is better compared to peers at 43% of domestic deposits, leading to cost of funds at 4.9%. Going forward, we believe the credit-cost trajectory over the medium term remains unclear due to the restructuring window and its ability to revive stressed exposures. The comfortable CET-1 ratio at 9.4% is better compared to peer banks, but equity raise may result in book value dilution. We maintain our Hold rating with a revised price target (PT) of Rs. 40.

Key positives

- The bank has made negligible COVID-related provisions so far but CET-1 ratio at 9.4% is better among PSU banks.
- PCR improved sequentially to 80.75%, an uptick of 135 bps. Due to the moratorium benefit, the quarter saw a sharp decline in slippage ratio to 1.51%, fall by 333 bps.

Key negatives

- Headline asset quality for the quarter deteriorated sequentially with its gross NPA at 14.11% (up from 13.8% in Q4FY2020).
- The moratorium book has not declined on a sequential basis, which is a dampener.

Our Call

Valuation - PNB currently trades at <0.5x its FY2022E book value, which reflects its weak asset-quality outlook and sluggish loan growth prospects. The NCLT-related resolution prospects at present appear bleak. The merger and stress on the overall book may keep the asset quality volatile during FY2021E. Though PNB's relatively higher CET-1 and CASA ratio are positives, a downside risk of asset-quality performance and book value dilution risk are still high. We maintain our Hold rating with a revised price target (PT) of Rs. 40.

Key Risks

An elongated or prolonged economic recovery or further stress due to the pandemic may result in spike in NPA and may affect profitability.

Valuation				Rs cr
Particulars	FY19	FY20	FY21E	FY22E
Net interest income (Rs. cr)	17,156	17,438	15,994	17,686
Net profit (Rs. cr)	-9,975	336	977	1,198
EPS (Rs.)	-46.9	0.5	1.5	1.8
PE (x)	NA	71.7	24.7	20.1
Book value (Rs./share)	89.5	87.7	88.8	90.3
P/BV (x)	0.4	0.4	0.4	0.4
RoE (%)	NA	0.6	1.6	1.9
RoA (%)	NA	0.0	0.1	0.1

Source: Company; Sharekhan estimates

Key result highlights from Concall

- ♦ **Restructuring:** Management estimates 5-6% of credit book to be restructured and expects to have clarity by September end based on Kamath Committee report. Once the account is restructured, it will reduce slippage risk. Management has clarity about SME, MSME, and retail loan due to RBI guideline and sees low probability of significant restructuring for these loans.
- ♦ **Asset-quality outlook:** Management anticipates around Rs. 8000 crore – 10,000 crore of slippages for FY2021. Housing loans would not come under restructuring though 5-6% of book may extend moratorium. No restructuring in corporate except government of India and another private (now non-operational) airlines account.
- ♦ **Sanctions and disbursement:** Sanction for the quarter stood at Rs. 10,000 crore and disbursement worth of Rs. 8,000 crore.
- ♦ **Pending provision:** Fraud provision is still pending, which PNB will have to provide in subsequent quarters. Moreover, there is expected to be ~Rs. 2,000 crores ageing provision per quarter.
- ♦ **Fraud accounts:** Provision up to Rs. 1,600 crores is remaining, which would be done during FY2021 for fraud accounts.
- ♦ **Asset monetisation:** On account of amalgamation, the bank is in position to sell few non-core assets worth Rs. 500 crore.
- ♦ **NIMs:** NIM for FY2021 is expected to be at 2.4-2.5%.
- ♦ **MSME sector:** At present, NPAs for the MSME sector were at 14.5% and are expected to be stable. Even after the ECLGC scheme, the scope of restructuring in MSME loans is low (as per management).
- ♦ **Sectors that will need restructuring:** The aviation sector in which the bank has primarily two large exposures, one being a PSU sector exposure which has Government of India (GoI) guarantees. The other, a non-functioning private airline, has already been restructured. Primarily, management expects hospitality, travel, and tourism as the main sectors, which may need restructuring.
- ♦ **BB and Below Book:** BB and below book of Rs. 40,000 crore are standard assets.
- ♦ **FITL:** The bank will be carving out the interest component of the moratorium loans under Funded Interest Term Loans (FITL) arrangement, which it will be carving out separately in September quarter.

Results

Particulars	Q1FY21	Q1FY20	YoY %	Q4FY20	QoQ %
Interest income	20604.9	13086.4	57.5	13,859.0	48.7
Interest expense	13856.5	8945.1	54.9	9,181.4	50.9
Net interest income	6748.4	4141.4	63.0	4,677.5	44.3
Non-interest income	3687.9	2075.3	77.7	2,529.3	45.8
Net total income	10,436.3	6,216.7	67.9	7,206.9	44.8
Operating expenses	5,156.3	2,735.2	88.5	3,274.6	57.5
Employee cost	3307.2	1681.7	96.7	1,853.8	78.4
Other costs	1849.1	1053.6	75.5	1,420.8	30.1
Pre-Provisioning Profit	5,280.1	3,481.4	51.7	3,932.3	34.3
Provisions	4685.9	2023.3	131.6	4,901.3	-4.4
Profit Before Tax	594.2	1,458.1	-59.3	-969.0	NA
Tax	285.71	439.5	-35.0	-271.8	NA
Profit after Tax	308.4	1,018.6	-69.7	-697.2	NA

Source: Company; Sharekhan Research

Restated Financials (Comparable basis)

					Rs cr
Particulars	Q1FY21	Q1FY20	YoY %	Q4FY20	QoQ %
Net interest income	6,748	6,240	8.1	6,810	(0.9)
Non-interest income	3,688	3,419	7.9	4,035	(8.6)
Net total income	10,436	9,659	8.0	10,845	(3.8)
Operating expenses	5,156	4,510	14.3	8,972	(42.5)
Employee cost	750	330	127.3	1,511	(50.4)
Other costs	4406	4180	5.4	7,461	(40.9)
Pre-Provisioning Profit	5,280	5,150	2.5	1,872	182.1
Provisions	4972	3940	26.2	12,005	(58.6)
Profit Before Tax	594	1,719	(65.4)	-10,563	NA
Tax	286	509	(43.8)	-430	NA
Profit after Tax	308	1,210	(74.5)	-10,133	NA

Source: Company; Sharekhan Research

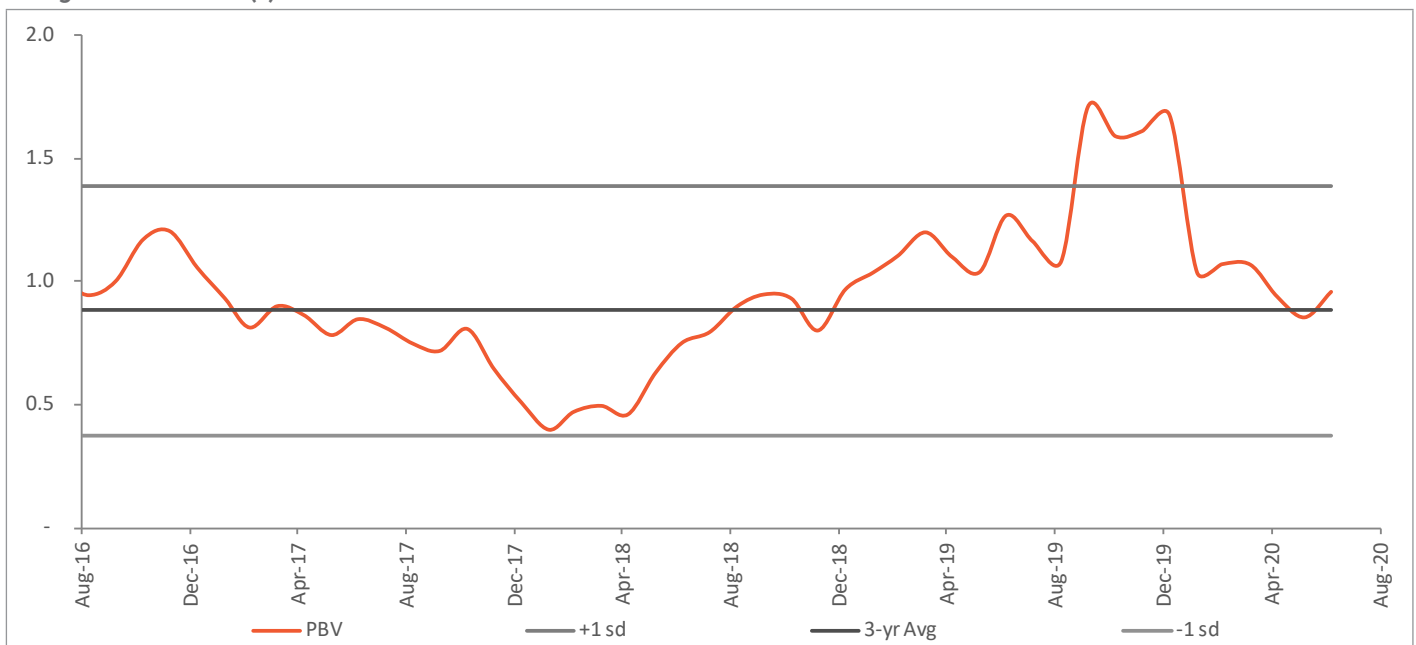
Outlook

While Q1 saw fewer NPA additions, this was largely due to the moratorium benefit extended to borrowers. Moreover, management has indicated that overall stress levels could increase post H1, which we believe would be an overhang on the stock. We believe there continues to be lot of uncertainty with regards to results. Credit cost is likely to depend on an economic recovery and resolutions of NCLT cases appear bleak for now. We believe due to weak credit demand and merger-related activities, credit growth will remain tepid for FY2021E. Moreover, due to the merger further integration and harmonisation issues, qualitative aspects may keep significant management bandwidth occupied, which will impact growth and profitability.

Valuation

PNB currently trades at <0.5x its FY2022E book value, which reflects its weak asset-quality outlook and sluggish loan growth prospects. NCLT-related resolution prospects at present appear bleak. The merger and stress on the overall book may keep the asset quality volatile during FY2021E. Though PNB's relatively higher CET-1 and CASA ratio are positives, a downside risk of asset-quality performance and book value dilution risk are still high. We maintain our Hold rating with a revised price target (PT) of Rs. 40.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Particulars	CMP	P/BV(x)		P/E(x)		RoA (%)		RoE (%)	
	Rs/Share	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E
Punjab National Bank	35	0.4	0.4	23.4	19.5	0.1	0.1	1.6	1.9
State Bank of India	201	0.8	0.7	14.3	8.1	0.3	0.5	5.5	8.7
Bank of India	48	0.4	0.4	27.1	9.3	0.2	0.3	2.3	2.7
Canara Bank	103	0.3	0.3	-27.2	9.8	-0.1	0.2	-1.0	3.4

Source: Company, Sharekhan research

About company

PNB is a government-owned bank with a network of ~6560+ branches, 9100+ ATMs, and 7,500+ business correspondents. The bank's majority presence is in Punjab, Haryana, Uttar Pradesh, Madhya Pradesh, and Bihar. More than 60% of its branches are in rural and semi-urban areas. PNB's gross advances were at Rs. 656,197 crores as on Q1 FY21. The bank has been rationalising its overseas operations, which have resulted into shrinking of overseas business. Domestic CASA ratio for the bank stands at 43.5% as of June 2020.

Investment theme

PNB has worked upon bringing significant improvement in the internal systems and processes post the discovery of frauds in one of its branches in 2018. The bank has restructured its processes, with a focus on recovery and resolution, hence taking stapes such as creating a stressed asset management vertical with dedicated team of over 2,700 employees, along with creating dedicated branches to focus on SME and retail disbursements. The bank has seen results of them, in terms of improved recovery. At present, the impact of COVID-19 and the resultant slow economic activity pose risks to borrowers' cash flows as well as on securities value. We believe the moratorium has further clouded the picture on asset quality and, therefore, we believe greater clarity will emerge post December. So far, the asset-quality outlook continues to be weak. Moreover, the NCLT process has been put on hold, which has further impacted recovery prospects.

Key Risks

An elongated or prolonged economic recovery or further stress due to the pandemic may result in spike in NPA and may affect profitability.

Additional Data

Key management personnel

Mr. S.S Mallikarjuna Rao	MD & CEO
Mr. P K Sharma	CFO/Chief General Manager
Mr Agyey Kumar Azad	Executive director
Mr Vijay Dube	Executive director

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Life Insurance Corp of India	3.6
2	HDFC Asset Management Co Ltd	1.2
3	Vanguard Group Inc/The	0.4
4	Dimensional Fund Advisors LP	0.2
5	SBI Funds Management Pvt Ltd	0.2
6	Kotak Mahindra Asset Management Co	0.1
7	FIL Ltd	0.1
8	FundRock Management Co SA	0.1
9	Norges Bank	0.1
10	Allianz SE	0.04

Source: Bloomberg

Sharekhan Limited, its analyst or dependant(s) of the analyst might be holding or having a position in the companies mentioned in the article.

Sharekhan

by BNP PARIBAS

Know more about our products and services

For Private Circulation only

Disclaimer: This document has been prepared by Sharekhan Ltd. (SHAREKHAN) and is intended for use only by the person or entity to which it is addressed to. This Document may contain confidential and/or privileged material and is not for any type of circulation and any review, retransmission, or any other use is strictly prohibited. This Document is subject to changes without prior notice. This document does not constitute an offer to sell or solicitation for the purchase or sale of any financial instrument or as an official confirmation of any transaction. Though disseminated to all customers who are due to receive the same, not all customers may receive this report at the same time. SHAREKHAN will not treat recipients as customers by virtue of their receiving this report.

The information contained herein is obtained from publicly available data or other sources believed to be reliable and SHAREKHAN has not independently verified the accuracy and completeness of the said data and hence it should not be relied upon as such. While we would endeavour to update the information herein on reasonable basis, SHAREKHAN, its subsidiaries and associated companies, their directors and employees ("SHAREKHAN and affiliates") are under no obligation to update or keep the information current. Also, there may be regulatory, compliance, or other reasons that may prevent SHAREKHAN and affiliates from doing so. This document is prepared for assistance only and is not intended to be and must not alone be taken as the basis for an investment decision. Recipients of this report should also be aware that past performance is not necessarily a guide to future performance and value of investments can go down as well. The user assumes the entire risk of any use made of this information. Each recipient of this document should make such investigations as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this document (including the merits and risks involved), and should consult its own advisors to determine the merits and risks of such an investment. The investment discussed or views expressed may not be suitable for all investors. We do not undertake to advise you as to any change of our views. Affiliates of Sharekhan may have issued other reports that are inconsistent with and reach different conclusions from the information presented in this report.

This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject SHAREKHAN and affiliates to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors. Persons in whose possession this document may come are required to inform themselves of and to observe such restriction.

The analyst certifies that the analyst has not dealt or traded directly or indirectly in securities of the company and that all of the views expressed in this document accurately reflect his or her personal views about the subject company or companies and its or their securities and do not necessarily reflect those of SHAREKHAN. The analyst further certifies that neither he or its associates or his relatives has any direct or indirect financial interest nor have actual or beneficial ownership of 1% or more in the securities of the company at the end of the month immediately preceding the date of publication of the research report nor have any material conflict of interest nor has served as officer, director or employee or engaged in market making activity of the company. Further, the analyst has also not been a part of the team which has managed or co-managed the public offerings of the company and no part of the analyst's compensation was, is or will be, directly or indirectly related to specific recommendations or views expressed in this document. Sharekhan Limited or its associates or analysts have not received any compensation for investment banking, merchant banking, brokerage services or any compensation or other benefits from the subject company or from third party in the past twelve months in connection with the research report.

Either SHAREKHAN or its affiliates or its directors or employees / representatives / clients or their relatives may have position(s), make market, act as principal or engage in transactions of purchase or sell of securities, from time to time or may be materially interested in any of the securities or related securities referred to in this report and they may have used the information set forth herein before publication. SHAREKHAN may from time to time solicit from, or perform investment banking, or other services for, any company mentioned herein. Without limiting any of the foregoing, in no event shall SHAREKHAN, any of its affiliates or any third party involved in, or related to, computing or compiling the information have any liability for any damages of any kind.

Compliance Officer: Mr. Joby John Meledan; Tel: 022-61150000; email id: compliance@sharekhan.com;

For any queries or grievances kindly email igc@sharekhan.com or contact: myaccount@sharekhan.com

Registered Office: Sharekhan Limited, 10th Floor, Beta Building, Lodha iThink Techno Campus, Off. JVLR, Opp. Kanjurmarg Railway Station, Kanjurmarg (East), Mumbai – 400042, Maharashtra. Tel: 022 - 61150000. Sharekhan Ltd.: SEBI Regn. Nos.: BSE / NSE / MSEI (CASH / F&O / CD) / MCX - Commodity: INZ000171337; DP: NSDL/CDSL-IN-DP-365-2018; PMS: INP000005786; Mutual Fund: ARN 20669; Research Analyst: INH000006183;

Disclaimer: Client should read the Risk Disclosure Document issued by SEBI & relevant exchanges and the T&C on www.sharekhan.com; Investment in securities market are subject to market risks, read all the related documents carefully before investing.