



3R MATRIX

	+	=	-
Right Sector (RS)	Green	Grey ✓	Red
Right Quality (RQ)	Green	Grey ✓	Red
Right Valuation (RV)	Green	Grey ✓	Red

+ Positive = Neutral - Negative

What has changed in 3R MATRIX

	Old		New
RS	Grey	↔	Grey
RQ	Grey	↔	Grey
RV	Grey	↔	Grey

Reco/View	Change
Reco: Hold	↔
CMP: Rs. 38	
Price Target: Rs. 42	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

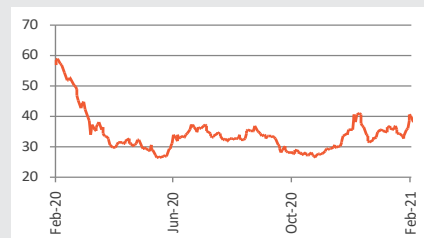
Company details

Market cap:	Rs. 42,015 cr
52-week high/low:	Rs. 59/26
NSE volume: (No of shares)	713.9 lakh
BSE code:	532461
NSE code:	PNB
Free float: (No of shares)	135.7 cr

Shareholding (%)

Promoters	76.9
FII	4.0
DII	10.6
Others	5.9

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	7.3	32.9	15.5	-33.6
Relative to Sensex	2.1	12.3	-19.0	-58.9

Sharekhan Research, Bloomberg

Summary

- Operational performance was reasonably strong, but asset-quality outlook continues to be uncertain.
- The Proforma Gross NPA and Proforma Net NPA ratio at 14.71% and 5.65%, respectively, are not materially ahead of reported numbers.
- Collections efficiency dipped in December, taking Q3 CE to 88%; but it was 92% till November.
- PNB currently trades at 0.8x/0.60x its FY2022E/FY2023E ABVPS, we maintain our Hold rating with a revised PT of Rs. 42.

Operational performance was reasonably strong for Q3FY2021. Net interest income (NII) came at Rs. 8,312 crore, down 1% q-o-q and was above expectations. PAT came at Rs. 506 crore, down 18% q-o-q, below expectations. Due to PNB's amalgamation (effective April 1, 2020) with erstwhile Oriental Bank of Commerce and United Bank of India, the quarterly/nine months results of the current financial year are not comparable with the corresponding year-ago period. Provisions were elevated, at Rs. 5,432.60 crore, up 31% y-o-y and 16%q-o-q, along with employee cost, which jumped by 67% y-o-y but down 10%q-o-q, which caused PAT to miss estimates. Proforma gross NPA and proforma net NPA ratio at 14.71% and 5.65%, respectively, are not materially ahead of reported numbers. The bank holds aggregate provision of Rs. 3,041.16 crore as of December 2020 (includes Rs. 446 crore for COVID-19 Regulatory Package Provision, Rs. 75 crore for OTR done under Resolution Framework for Covid-19 related stress, and Rs. 2,520 crore), which is ~11% of reported NNPA. Provision Coverage Ratio (PCR) as of December 31, 2020, works out to 85.16%. Restructured book (under Covid-19) stood at Rs. 11,998 crore or 1.82% of loans. The one-time MSME restructured book is at Rs. 3,071 crore versus Rs. 2,713 crore, up 13.2% q-o-q. Standard restructured book stood at Rs. 2,267 crore versus Rs. 2,339 crore, down 3.1% q-o-q. The total standard restructured book at 0.34% stands against 0.36% q-o-q. The bank reported pro-forma slippages of ~2%, restructured loans of 2.5%, and has combined coverage of ~60% on its entire stress pool. Hence, we have revised our estimates, but we believe asset-quality wise, the outlook still lacking clarity. We maintain our Hold rating with a revised PT of Rs. 42.

Key positives

- Reported asset quality improved with GNPA/NNPA improving to 12.99%/4.03% as against 13.43%/4.75% in Q2FY2021. However, there is low visibility on asset-quality outlook.

Key negatives

- Business momentum was subdued with deposits growing by 1.2% q-o-q & advances growing 1.5% q-o-q.
- Global NIM declined to 3.09% (down from 3.21% in Q2FY2021).

Our Call

**Valuation** - PNB currently trades at 0.8x/0.60x its FY2022E/FY2023E adjusted book value, which reflects its weak asset-quality outlook and sluggish loan growth prospects. We believe NCLT-related resolutions (but recovery prospects in FY2022E) but expected weak trends in asset quality of corporate and SME segments would keep asset-quality outlook volatile during FY2021E. We maintain our Hold rating with a revised price target (PT) of Rs. 42.

Key Risks

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

Valuation

Particulars	FY19	FY20	FY21E	FY22E	FY23E
Net interest income	17,156	17,438	27,503	31,023	36,850
Net profit (Rs. cr)	-9,975	336	2,817	4,978	6,776
EPS (Rs.)	-46.9	0.5	3.0	5.3	7.2
PE (x)	NA	76.2	12.7	7.2	5.3
ABVPS (Rs.)	NA	5.8	30.3	47.9	67.6
P/ABV (x)	NA	6.6	1.3	0.8	0.6
RoE (%)	NA	0.6	3.9	5.8	7.5
RoA (%)	NA	0.0	0.2	0.3	0.4

Source: Company; Sharekhan estimates

## Key Concall Highlights

**Stressed asset book:** PNB has made 15% of provisions for stressed assets and not taken in interest income.

**Credit cost** stood at 2.02% at December end. Including provisions made for proforma NPA, credit cost goes to 2.5%.

**Credit Cost Guidance:** Earlier the bank had given guidance that credit cost will be ~2.5% till March 2021, but it has already reached that in Q3 itself. In FY2022E, credit cost is likely to be 1.25-1.5%; management has maintained its guidance.

**Restructured book** (invocation) is at Rs. 11,998 crore. Only for MSME PNB has done Rs. 968 crore, and will be doing ~Rs. 1,000 crore additional in Q4 (likely). Rs. 12,500-13,000 crore will be overall restructuring in FY2021E end.

**Slippage guidance** earlier given in Rs. 12,000 crore; Management expects recovery and upgrades in Q4.

**Tax rate:** There was a DTA reversal impact so the tax rate was high. ETR normalised in line with other banks at ~34%.

**Treasury Income:** PNB expects another Rs. 800 crore in Q4FY2021E. Management expects bond yields will be tapering off, as the RBI has already started OMO.

**Advances growth:** Huge investment planned in the economy post the budget. Corporate credit demand was muted as no new capex/investments were coming. By Q4FY2021, credit growth will be 4% y-o-y, where only 1% is done till December. By FY2022E, management expects 10% credit growth for PNB.

**CE** in December was muted, but it was 92% till November. PNB expects CE in JFM to go above 94%. For Q3, it was ~88%.

**Slippage outlook:** Management would like to control slippage for H2, but it has guided to have around Rs. 12,000 crores restructured assets for FY2021.

**One-time Restructuring (OTR)** provided for 50%; Rs. 1,000 crore will be provision requirement in the restructured book in FY2022E.

**MSME and retail will see higher slippage** in Q4FY2021. Out of Rs. 4,000 crore, around Rs. 1,000 crore may slip in Q4. Management does not expect material slippage in the corporate segment in Q4.

**SMA 1 and 2** are high in 9M period, and hence not disclosed. PNB expects the number to be more normalised in Q4FY2021. At the end of June, SMA 2 was at Rs. 15,000 crore and is in the normal range.

**Capital Issue:** QIP was not fully subscribed. PNB received Rs. 3,788 crore, but green shoe option did not come in. Management will come to market again at an appropriate time.

**Recovery pipeline:** Q4 marked 17 accounts with cash recovery of Rs. 3,400 crore. Management expects recovery of Rs. 1,600 crore (exposure is Rs. 3,688 crore) in DHFL, but it can come in Q4 or Q1FY2022.

**SMA 1 and 2:** Management has already shared proforma GNPA and restructuring figure. Generally, SMA2 stands at Rs. 15,000 crore-16,000 crore.

**Proforma slippage breakup:** Agri is Rs. 2,182 crore; MSME is Rs. 6,049 crore; Retail is Rs. 2,798 crore; and other is Rs. 1,890 crore.

**Staff cost:** Management has fully taken the wage hike impact in Q3.

**Branch rationalisation:** PNB has identified 500 branches for rationalisation. By March, management will do half and remaining by June; it will mostly be in the southern part of the country.

**Provision for OTR** taken included for proforma NPAs Rs. 11,030 crore, majority is standard assets. For Q4, Rs. 1,000 crore of provisions will need to be done for invoked but not provided accounts.

**Slippage guidance:** Management had earlier given slippage guidance of Rs. 10,000 crore for H2, which the bank expects will cross. For Q3, it is Rs. 125 billion, but total of Q3 and Q4 will be Rs. 130 billion.

**Recovery:** SREI infra and SREI assets will be taken as the account is under stress and will get clarity by March 2021.

**Subsidiary assets:** PNB has already sold off UTI AMC stake. Management expects proceeds from real estate worth Rs. 500 crore by June 2021. Insurance subsidiary has 30% share and would like to list them first. So, currently it continues to hold stake in those companies.

Results				Rs cr	
Particulars	Q3FY21	Q3FY20	y-o-y (%)	Q2FY21	q-o-q (%)
Interest income	20324.7	13562.7	49.9	20945.8	-3.0
Interest expense	12011.7	9207.6	30.5	12552.6	-4.3
<b>Net interest income</b>	<b>8313.0</b>	<b>4355.1</b>	<b>90.9</b>	<b>8393.2</b>	<b>-1.0</b>
Non-interest income	2973.9	2404.8	23.7	2492.7	19.3
Net total income	11286.8	6759.9	67.0	10885.9	3.7
Operating expenses	4896.0	2997.0	63.4	5211.0	-6.0
<b>Pre-provisioning profit</b>	<b>6390.8</b>	<b>3762.9</b>	<b>69.8</b>	<b>5674.9</b>	<b>12.6</b>
Provisions	5432.6	4146.0	31.0	4696.2	15.7
Profit before tax	958.2	-383.1	N.A	978.8	-2.1
Tax	452.18	109.1	314.3	358.0	26.3
<b>Profit after tax</b>	<b>506.0</b>	<b>-492.3</b>	<b>N.A</b>	<b>620.8</b>	<b>-18.5</b>

Source: Company; Sharekhan Research

## Outlook and Valuation

### ■ Sector view - Headwinds continue for PSU banks

The economy is showing signs of a gradual recovery, which augurs well for long-term demand outlook. However, potential risks due to stress in the economy along with uncertainty on COVID-19 related developments continue to pose a challenge, especially for PSU banks. While recent regulatory measures have cushioned earnings (especially on the asset-quality recognition part) and the gradual return to normalised business traction will be positive for BFSI companies, we believe capital-constrained PSU banks, which are still burdened with legacy NPAs, may take longer to recover. Hence, near-term return ratios may remain weak. However, in this scenario, well-capitalised banks may utilise this opportunity to gain market share from weaker PSU banks.

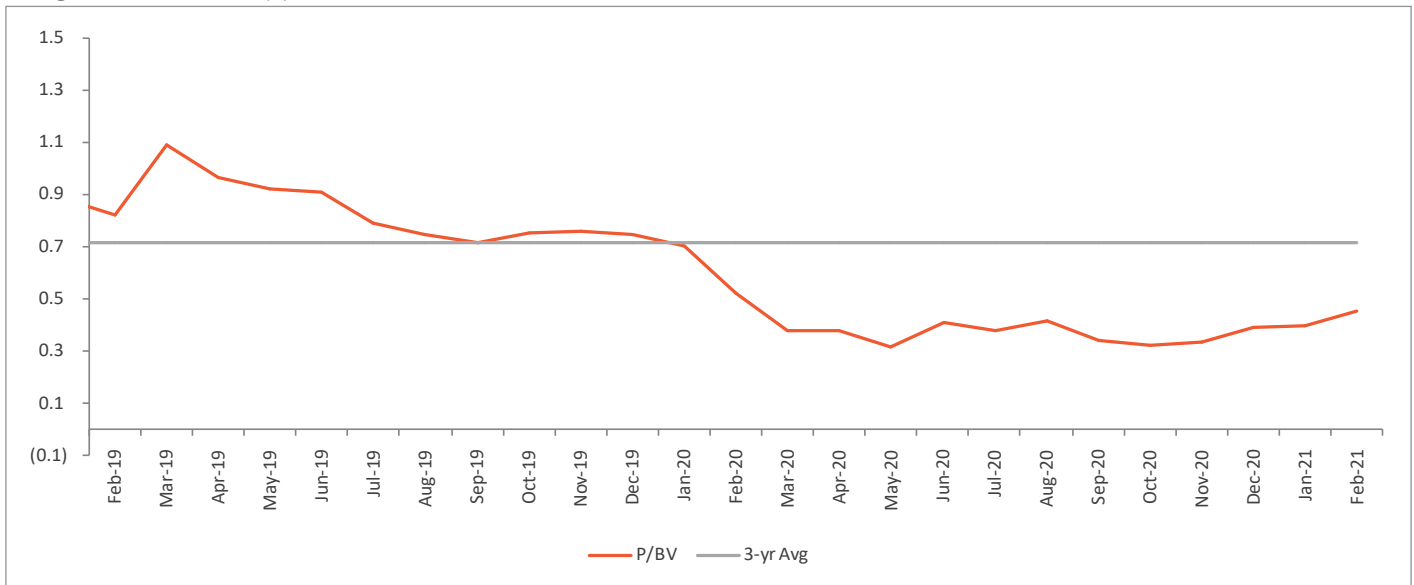
### ■ Company outlook - Long road to normalcy

PNB posted reasonably strong results on operational basis, but they were helped by the standstill on NPA recognition. However, asset-quality outlook remains a challenge and key monitorable. PNB posted elevated provision levels, which declined by 3% y-o-y, but were up 16% q-o-q. Deposits growth was 1% y-o-y, with CASA growth at ~5%, driven by strong growth in savings deposits (8% y-o-y). Consequently, CASA ratio improved to 44%. The decline in cost of funds (CoF) continued, which was positive, and cost of deposits were at 4.2%, down 25 bps q-o-q/100 bps y-o-y, with NIM at 3.1% (-10 bps q-o-q). The bank's recent capital raise has improved its CET-1 ratio to 10.1% (up 60 bps q-o-q). High SMA amounts as well as continued slippage/credit cost expectation cloud asset-quality outlook visibility. The bank has reduced its liability pricing, but softening yields and slow credit growth may keep NIM performance muted, predicated on slippages pace in H2FY2021. We believe the road to normalcy is still a long one for PNB.

### ■ Valuation - Maintain our Hold rating with revised a PT of Rs. 42

PNB currently trades at 0.8x/0.60x its FY2022E/FY2023E adjusted book value, which reflects its weak asset-quality outlook and sluggish loan growth prospects. We believe NCLT-related resolutions (but recovery prospects in FY2022E) but expected weak trends in asset quality of corporate and SME segments would keep asset-quality outlook volatile during FY2021E. We maintain our Hold rating with a revised PT of Rs. 42.

#### One-year forward P/BV (x) band



Source: Sharekhan Research

#### Peer valuation

Particulars	CMP (Rs / Share)	P/BV (x)		P/E (x)		RoA (%)		RoE (%)	
		FY21E	FY22E	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E
Punjab National Bank	38	1.25	0.79	12.7	7.2	0.2	0.3	3.9	5.8
State Bank of India	397	1.54	1.40	22.6	15.0	0.4	0.5	7.9	10.4
Bank of India	59	0.50	0.49	102.2	10.3	0.2	0.4	-2.8	4.6

Source: Company, Sharekhan Research

## About company

PNB is a government-owned bank with a network of ~10,925+ branches, 13900+ ATMs, and 12,346 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. 705,956 crore as of Q3FY2021. The bank has been rationalising its overseas operations, which have resulted into shrinking of its overseas business. Domestic CASA ratio for the bank stands at 44.7% as of December 2020.

## Investment theme

PNB has worked upon bringing significant improvement in its 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 steps such as creating a stressed asset management vertical with a dedicated team of over 2,700 employees, along with creating dedicated branches to focus on SME and retail disbursements. The bank has seen results from 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 asset-quality picture still lacks clarity.

## Key Risks

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

## Additional Data

### Key management personnel

Mr. S.S Mallikarjuna Rao	MD & CEO
Mr.Sanjay Kumar	Executive director
Mr Agyey Kumar Azad	Executive director
Mr Vijay Dube	Executive director

Source: Company

### Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Life Insurance Corp of India	3.77
2	Vanguard Group Inc/The	0.33
3	Nippon India Life Asset Management	0.23
4	Dimensional Fund Advisors LP	0.21
5	Kotak Mahindra Asset Management Co	0.18
6	SBI Funds Management Pvt Ltd	0.16
7	HDFC Asset Management Co Ltd	0.12
8	ICICI Prudential Asset Management	0.11
9	FundRock Management Co SA	0.07
10	Norges Bank	0.06

Source: Bloomberg

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## Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and deteriorating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

# Sharekhan

by BNP PARIBAS

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