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Equity Research Pakistan

In Focus

Banks

Marketweight

NBP - REDUCE

Fair Value: PKR 61

Current Price: PKR 62

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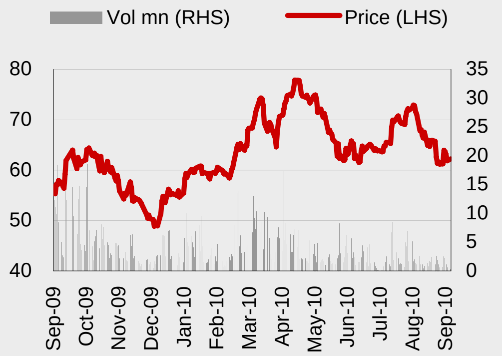
Stock Statistics

Ticker		NBP
Mkt Cap	USD mn	975
12M ADT	mn shares	4.2
Shares Outstanding	mn	1,345

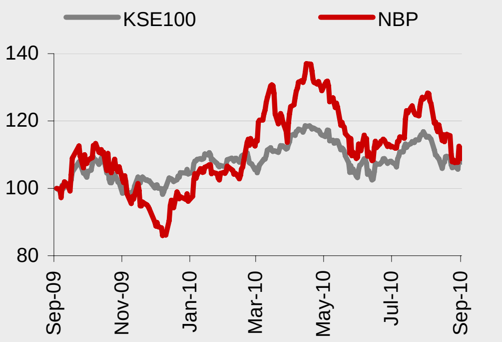
Stock Performance

	1M	3M	12M
Absolute %	-12.6	-1.6	9.4
Relative to KSE %	-7.2	-2.9	1.0

Price and Volume Graph



NBP vs KSE100 Relative Index Chart



Fragile Recovery: Still Not Impressed

- **NBP posted PAT of PKR7.8bn (EPS 5.81) for 1HCY10, depicting a healthy 25% YoY growth**
- **On the positive side, NBP surprisingly booked reversals in NPLs which declined by 4% QoQ to PKR69.7bn. Infection ratio has also improved to 13.4% in Jun10 from 14.1% recorded in Mar10. Due to higher exposure in commodity financing, other agri-related loans and textile, we remain pessimistic on asset quality for NBP as post flood impact is yet to be booked**
- **Rationalizing cost of funds (-6bps) and improved earning asset yields helped increase margins by 8bps QoQ**
- **We expect asset quality concerns to overshadow positive impact of non interest income and margins and revise CY10 EPS forecast and Target price down by 3% and 1% respectively**
- **NBP currently trades at PBV multiple of 0.67x compared to an average of 0.9x for the banking sector and offers a meager 1% upside to our TP of PKR61/sh (avg. of PBV, DDM & RIVM). Considering declining ROE with asset quality concerns, we maintain a cautious stance on the scrip**

NBP posted PAT of PKR7.8bn (EPS 5.81) for 1HCY10, depicting a healthy YoY growth of 25%. Profitability emerged through sizeable recovery in NPL provisions, lower cost of fund and improved non interest income. However, delinquencies of investment portfolio (significant surge in diminution losses) together with higher admin charges limited full swing recovery.

Going forward, we expect asset quality concerns to overshadow positive impact of non interest income and margins. We thus revise our CY10 EPS forecast and Target price down by 3% and 1% respectively.

NBP1HCY10 Result Review

PKR mn	1HCY10	1HCY09	YoY	2QCY10	2QCY09	YoY
NII	20,738	18,979	9%	10,686	9,513	12%
Provisions	4,459	5,581	-20%	2,520	3,875	-35%
Non int. income	8,300	6,967	19%	4,300	3,308	30%
Non int. expenses	12,929	10,681	21%	7,120	5,560	28%
PAT	7,821	6,276	25%	3,605	2,067	74%
EPS	5.81	4.66	25%	2.68	1.54	74%

Source: BMA Research

Diminution in investment countered recovery in provision losses

On the positive side, NBP surprisingly booked reversals in NPLs which declined by 4% QoQ to PKR69.7bn. Infection ratio has also improved to 13.4% in Jun10 from 14.1% recorded in Mar10. Nonetheless, this development seems short lived as recent flood is set to trip-up the aforesaid recovery. Although NBP has shed PKR15bn from loan portfolio since Dec-09, pre-flood loan accumulation for

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commodity financing and higher exposure to textile sector is likely to remain vulnerable in the short term. We thus remain pessimistic on asset quality for NBP for the rest of CY10.

Despite prudent reshuffling of investments, focus on T-bills and reduction in exposure to TFCs, provision for diminution of investment surged to PKR1.57bn during 2QCY10. We believe this to be a result of declining equity prices – transmitted through equity portfolio built up by redeeming NIT-LOC units.

Rationalizing cost of funds helped improve margins

NBP has shown considerable improvement towards reduction in cost of funds during 2QCY10. With favorable sector deposit growth during 2Q, NBP compressed fixed deposits by 8% QoQ while achieving accumulation of saving and current deposits (37% and 17% QoQ respectively). This led to 14% QoQ growth in deposits while cost has reduced by 6bps QoQ. On the other hand, interest rate reversal has also jacked up earning yields on assets resulting in margins to swell up by 8bps on quarterly basis.

Considering weak credit creation, seasonal deposit outflows and delays in foreign inflows, sustainability of deposit growth and cost controls seem challenging for 2HCY10. However increasing interest rates scenario suggests sustained margins.

Non interest income surge by PKR1.3bn

Non interest income increased by PKR1.3bn compared to the corresponding period last year, primarily on account of healthy trading gains, dividends and fee/commission income.

On account of earlier announced appraisals and pension benefits, administration cost increased by 21% YoY in Jun10. We increase our annual forecast for pay benefits by 3pps to 15% for CY10.

Weak fundamental & fragile recovery: Caution maintained

NBP currently trades at PBV multiple of 0.67x compared to an average of 1x for the banking sector and offers a meager 1% upside to our TP of PKR61/share (avg. of P/B, DDM & RIVM). While we have a Hold stance on the stock, we highlight our concerns on asset quality and declining ROE; advice caution in the stock.

NBP: Financial highlights

(PKR mn)	2008E	2009F	2010E	2011F	2012F
Net int. income	37,058	38,458	41,835	43,216	47,997
Prov. & write offs	10,971	11,669	10,636	8,713	6,709
Other income	16,414	19,023	17,038	19,326	22,965
Non int. expense	19,502	23,514	26,732	30,544	34,900
Profit after tax	15,457	18,209	14,244	15,440	19,412
EPS (PKR)	11.49	13.53	10.59	11.48	14.43
DPS (PKR)	6.50	7.50	5.00	6.00	7.00
ROE	14.1%	16.4%	11.6%	11.9%	13.9%
ROA	2.0%	2.1%	1.5%	1.4%	1.6%

Source: BMA Research

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