# National Bank of Pakistan

## Estimates upgraded on change in asset and liability mix

Research Entity Notification Number: REP-005

Wednesday March 30, 2016

**NBP - Overweight**

**Target Price: PKR 63**

**Current Price: PKR 51**

**NBP Performance**

| | 1M | 3M | 12M |
|---|---|---|---|
| Absolute % | 3% | 9% | 16% |
| Relative to KSE % | -2% | 9% | 6% |

Source: PSX, BMA Research

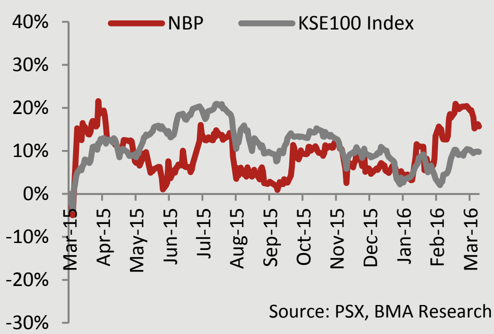
| | |
|---|---|
| Bloomberg | NBP.PA |
| Reuters | NBPK KA |
| MCAP (USD mn) | 1,044 |
| 12M ADT (USD mn) | 1.5 |
| Shares Outstanding (mn) | 2,128 |

**NBP: Earning Estimates**

| (PKR) | CY16F | CY17F | CY18F | TP |
|---|---|---|---|---|
| **New** | 9.0 | 9.3 | 10.2 | 63 |
| **Old** | 8.4 | 8.8 | 9.5 | 59 |
| **Change** | 7% | 6% | 6% | 7% |

Source: BMA Research

**Relative Chart KSE-100 vs NBP**




Source: PSX, BMA Research

**National Bank Of Pakistan's (NBP) CY15 earnings at PKR19.2bn (EPS: PKR9.03) surprised the street with the bank also posting tangible improvements in the balance sheet. NBP's deposit growth of 16%YoY far outpaced the industry growth of 12.5%YoY while its current accounts posted a growth of 23%YoY. The asset mix continues to remain skewed towards government securities (IDR: 56%), in line with the industry trend. However the bank's fixed income portfolio is now more concentrated in short duration government T-bills, constituting ~62% (CY14: 26%) of overall fixed income portfolio. In a more recent development, NBP was served a notice by US banking regulator over incompliance with certain AML regulations. In this regards, the bank has been given 60 days to address all the deficiencies and gain compliance. To note, US operations constitute roughly 2% of bank's total asset base and is currently not breaking-even. However, mitigating the downside in earnings are i) higher than earlier anticipated growth in advances and ii) improved deposit mix. Consequently, we have upward revised our earnings estimates by 6%-7% over our investment horizon to account for higher than expected deposits and advances growth. Consequently our TP has been revised to PKR63/sh. The scrip trades at CY16F forward P/B and P/E multiples of 0.67x and 5.72x, respectively. Overweight**

**Encouraging accumulation of cost free deposits:** NBP saw a robust growth in its deposits (~16%), outperforming the industry's overall growth of 13%YoY in deposits during CY15. Dissecting the deposit growth further, the cost free CA posted a growth of 23%YoY which allowed the bank to keep its CASA mix steady at ~77% in CY15. Going forward, we have assumed the bank to maintain its current market share of deposits and forecast CASA to improve to 78% by CY20.

**Reshuffle in the duration of fixed income portfolio:** NBP bond portfolio underwent a major shift in its duration profile as the bank shed its long duration PIBs in favor of short term T-bills in CY15. Consequently the concentration of PIBs which had stood at 65% in CY14 has now reduced to 36% in CY15 of its overall fixed income portfolio. Furthermore, from the bank's overall PIB portfolio, we estimate that PKR120bn-PKR125bn is up for maturity in CY16, which will likely put a downward pressure on NIMs, expected to shrink to 3.5% (CY15: 4.0%)

**Expect a double digit growth in loan book:** With a CAR of ~17.5% and coverage of ~90%, the bank has adequate space on its books to tap local advances growth. There have always been concerns over the bank's risk management policies, underscored by its high infection ratio (~18.4%). The yearly incremental NPL since CY11 has on average stood at 0.5% after removing one outlier of 3.7% in CY13 (with outlier, 1.18%), while the loan growth has averaged around 6%-7% over the same period. Going forward, we have conservatively assumed incremental infection ratio at ~1.3% with a loan growth averaging around 13%, over the period CY16- CY20. This is in contrast to our previous loan growth estimates of 11%. Any increase in incremental NPLs from estimated levels will result in downward revision of our earnings estimates

**A rendezvous with US regulator:** NBP was recently served a notice by Federal Reserve of New York and NYSDFS over incompliance with certain AML regulations. In this regards, the bank has been given 60 days to address all the deficiencies and gain compliance. To note, US operations constitute roughly 2% of bank's total asset base and is currently not breaking-even. As per our discussion with the management, the bank is actively working with the regulator and expects to achieve the compliance with all relevant regulations within due course.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**Investment Perspective:** Tweaking our estimates of asset and liabilities mix, we have upward revised our earnings estimates by 6%-7% over our investment horizon and consequently our TP has been revised to PKR63/sh (upside 24%). In addition, the scrip also offers an attractive D/Y of ~15% on last closing. The scrip trades at CY16F forward P/B and P/E multiples of 0.67x and 5.72x respectively. Overweight

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| **Rating definitions** | |
|---|---|
| Overweight | Total stock return > expected market return + 2% |
| Market-weight | Expected market return ± 2% |
| Underweight | Total stock return < expected market return - 2% |

*Total stock return = capital gain + dividend yield

Old rating system (discarded effective Feb 29'16)

| | |
|---|---|
| Buy | >20% upside potential |
| Accumulate | >=5% to <=20% upside potential |
| Hold | <5% to >5% potential |
| Reduce | <=-5% to >=-20% downside potential |
| Sell | <-20% downside potential |

## Valuation Methodology

To arrive at our period end target prices, BMA Capital uses different valuation methodologies including

- Discounted cash flow (DCF, DDM)
- Relative Valuation (P/E, P/B, P/S etc.)
- Equity & Asset return based methodologies (EVA, Residual Income etc.)