

Company Report

Wednesday, September 11, 2024

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COMPANY UPDATE

National Bank of Pakistan (NBP)

Commercial Banks

Recommendation	BUY
Target Price: Jun-25	82.6
Last Closing: 10-Sep-24	59.2
Upside (%):	40%
Valuation Methodology:	Justified P/B

Market Data

Bloomberg Tkr.	NBP PA
Shares (mn)	2,128
Free Float Shares (mn)	509.26
Free Float Shares (%)	24%
Market Cap (PKRbn)	125.97
Market Cap (USDmn)	452.08
Exchange	KSE-100

Price info.	01M	03M	09M	12M
Abs. Return	25%	61%	101%	172%
Low	43.4	33.5	28.0	21.3
High	63.0	63.0	63.0	63.0

Key Company Financials

Period End: Dec

PKRbn	CY23A	CY24E	CY25F	CY26F
Total Revenue	169	146	141	162
Net Income	52	21	35	46
EPS (PKR)	24.37	9.66	16.67	21.39
DPS (PKR)	-	5.00	8.50	14.00
Total Assets	2,178	2,396	2,635	2,899
Total Equity	383	393	410	426

Key Financial Ratios

ROE (%)	15%	6%	9%	12%
P/E (x)	2.43	6.13	3.55	2.77
P/B (x)	0.33	0.32	0.31	0.30
DY (%)	0%	8%	14%	24%

Source: Bloomberg, CapitalStake, PSX, Company Financials, IGI Research

Commercial Banks

NBP: Closure of Pension Case and Expected Dividend Revival to Unlock Value

- We initiate coverage on NBP with a 'BUY' rating and target price of PKR 82.6/share offering 40% upside from last close. We base our investment thesis on a) Settlement of pension case, b) Resumption of Dividends, c) Strong Capital Position, d) Asset Quality Risks remain well-managed e) maintaining a low cost deposit profile and f) Attractive valuations with Discounted P/B compared to peers.
- Although NBP suspended dividend payouts in 2016 on prudent basis, the Bank previously remained one of the highest dividend paying stocks. The settlement of the pension payments and availability of abundant capital reserves has increased the prospects of resumption of dividend payouts.
- Using Justified P/B approach, we have a 'BUY' rating on NBP with a Jun-25 target price of PKR 82.6/share offering a ~40% upside from the last closing price of PKR 59.2/share (10-Sep-24). The Bank is currently trading at FY25/26 P/B of 0.31/0.30 with an expected CY25F dividend yield of 14%.

Initiating Coverage on National Bank of Pakistan (NBP) with "BUY" rating

We initiate coverage on NBP with a 'BUY' rating and target price of PKR 82.6/share offering 40% upside from last close. NBP is one of the largest lending institutions with 1,508 operating branches. The Federal Government holds 75.6% shares of the bank and has recently been made part of Pakistan Sovereign Wealth Fund. The Bank also acts as an agent to SBP and handles treasury transactions for the Government of Pakistan.

We base our investment thesis on a) Settlement of pension case, b) Resumption of Dividends, c) Strong Capital Position, d) Asset Quality Risks remain well-managed e) maintaining a low cost deposit profile and f) Attractive valuations with Discounted P/B compared to peers.

Recommendation: Using Justified P/B approach, we have a 'BUY' rating on NBP with a Jun-25 target price of PKR 82.6/share offering a ~40% upside from the last closing price of PKR 59.2/share (10-Sep-24). The Bank is currently trading at FY25/26 P/B of 0.31/0.30 with an expected CY25F dividend yield of 14%.

Key Catalyst: Key catalysts include a) Increase in Non-Interest Income, b) Accumulation of low cost deposits and c) Growth in private sector borrowings as economy picks up.

Key Risk: Key risks include, a) Asset Quality Risks such as increase in Non-performing loans, b) Implementation of IFRS-9 and c) Imposition of additional tax on ADR below 50%.

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Important Disclosures at the end of this report

 A Packages Group Company

Investment Thesis

1. Settlement of Pension Case

About the Case

In 1977, the Federal Government through Pakistan Business Council, directed all the nationalized banks to provide pensions capped at 70% of the last drawn salary. In 1997, the Pakistan Business Council was abolished and the Board of Directors of the Bank were authorized to determine the personnel policies relating to the remuneration and benefits of the employees. By virtue of this, the Board of NBP revised upwards the basic salary by 110%-140% while reducing the pension benefits to 33% of the last drawn salary. However, since 2010-11, NBP has been served with litigations by employees demanding pensions to be paid on the 1977 directive.

In March 2024, a ruling was made on the pension case requiring the bank to pay PKR 60bn in pension liabilities. However, according to a press release published by the bank, the final settlement amount was settled at PKR 49bn which the bank recorded in 2QCY24 leading to a per share impact of ~PKR 12/share while the future recurring pension expense will be disclosed in due course. With the pension case now settled, bank's earnings are expected to rebound with strong prospects of dividend payouts.

2. Resumption of Dividends

Although NBP suspended dividend payouts in 2016 on prudent basis, the Bank previously remained one of the highest dividend paying stocks. The settlement of the pension payments and availability of abundant capital reserves has increased the prospects of resumption of dividend payouts. We anticipate a dividend payout of PKR 5/share in CY24 which is expected to gradually increase to their historical average payout of 70-80% leading to forecasted CY25F D/Y of ~14%.

3. Strong Capital Position

The Bank has not paid any dividends since 2016 awaiting the outcome of the pension case, which has resulted in a significant increase in the bank's Tier 1 CAR and total CAR from 11.66% and 16.5% to 19.8% and 25.5% respectively in CY23. Although the recent verdict regarding the pension case under which NBP paid off a large sum as one-time pension payment lowered NBP's Tier 1 and total CAR to 18.62% and ~24.7% in 2QCY24, it still comfortably meets the minimum regulatory requirement of 10.5% and 14% respectively.

Exhibit: Equity and ROE comparison

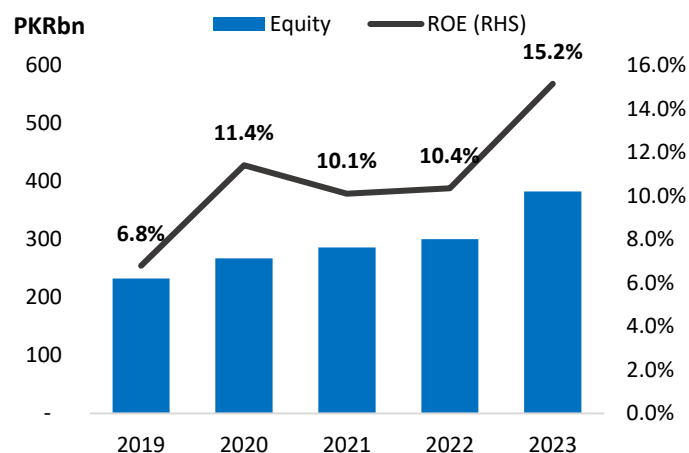
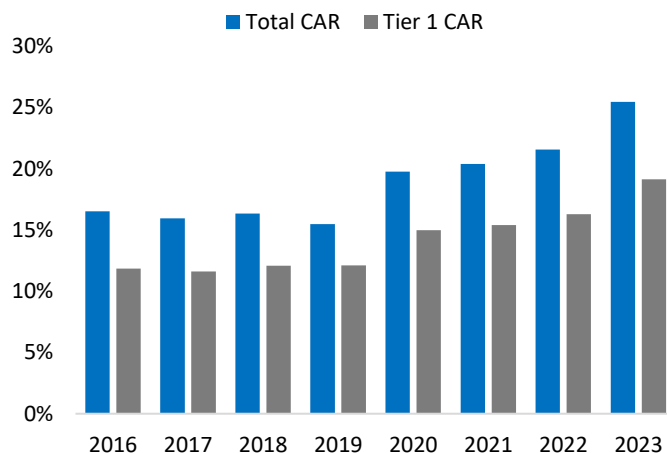


Exhibit: Total CAR and TIER 1 CAR from 2016-2023



Source: Company Accounts, IGI Research

4. Asset Quality Risks Remain Well-Managed

Historically, NBP has served as a major lender to companies mainly in the power, metals, textile, oil and gas sectors with over 30% of the non-performing loans coming from the textile and metal products sectors. The bank has had an average infection ratio of ~14% from CY20-23 which is relatively higher as compared to the banking sector average of ~5-10%. However, in CY23, NBP has shifted its exposure more towards the oil and gas sector, which can lead to some reduction in the Bank’s NPLs as suggested by a slight decrease of 1.1% in 1HCY24. In CY23, the Bank’s ADR ratio stood at 44% which has decreased to 38% in 1HCY24, the Bank is confident to increase its ADR ratio between 40-50% by the end of CY24 to avoid ADR-related taxation.

Over time, NBP has gradually increased its IDR from 60% in CY20 to 120% in CY23 with investments mainly concentrated in Government securities such as PIBs and T-Bills. In 1HCY24, the Bank’s investment portfolio consisted of 69% in PIBs and 27% in T-Bills. Moreover, the bank has focused on investing in shorter duration securities in the inverted yield curve environment. Going forward, we believe investments to be directed towards longer term maturities with the expected decline in interest rates.

Exhibit: NBP's NPLs and Coverage Ratio

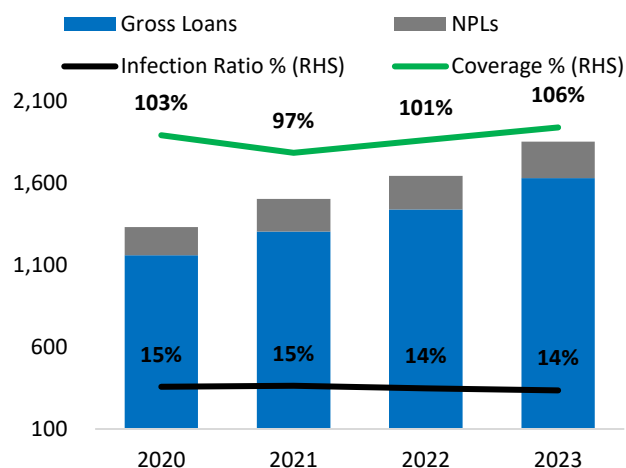
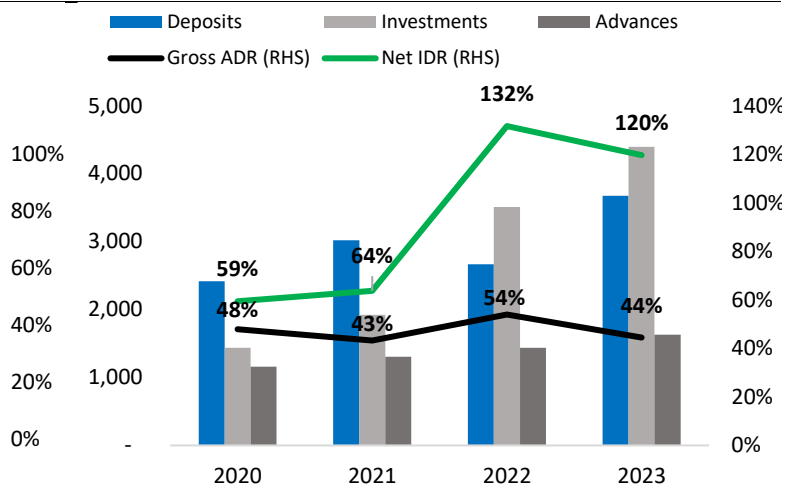


Exhibit: NBP's Deposits, Investments and Lending



Source: Company Accounts, IGI Research

Exhibit: NBP's Advances by Industry Sector

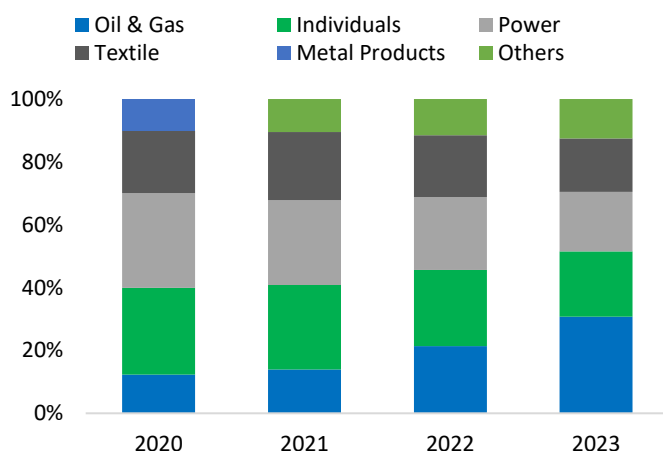
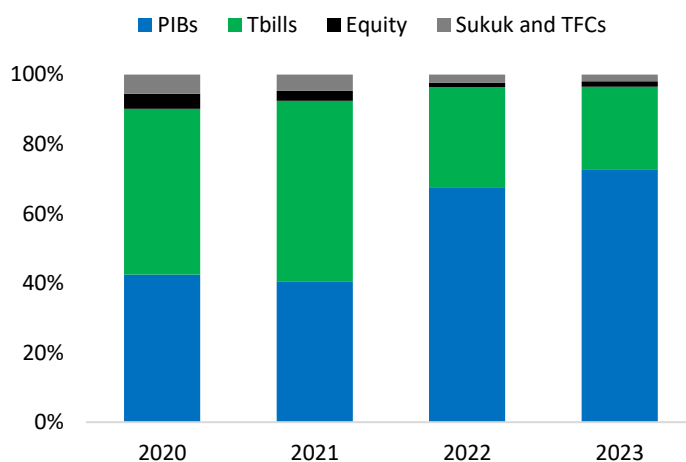


Exhibit: NBP's Investment Portfolio



Source: Company Accounts, IGI Research

5. Maintaining a Low Cost Deposit Profile

The Banking sector deposits have been growing at an average rate of 13% from CY20-23, while NBP's average share in total sector deposits has remained between 12-14%. We anticipate the bank's deposits growth to be in line with industry trends averaging around 12-15% from CY25-28.

NBP has mainly focused on maintaining a low cost deposit base with the CASA ratio increasing to 82% in 1HCY24 from 79% recorded at the end of CY23. This ratio is consistent with the CASA ratio of ~83% of KSE-100 banking sector however higher than IGI's banking sector universe average CASA ratio of 79.7%. Moreover, the bank's term deposits share have

declined to 18% in 1HCY24 from 20% in CY23 whereas the proportion of current accounts have remained flat at 56%.

Exhibit: Deposits of IGI Banking Sector Universe (PKRbn)

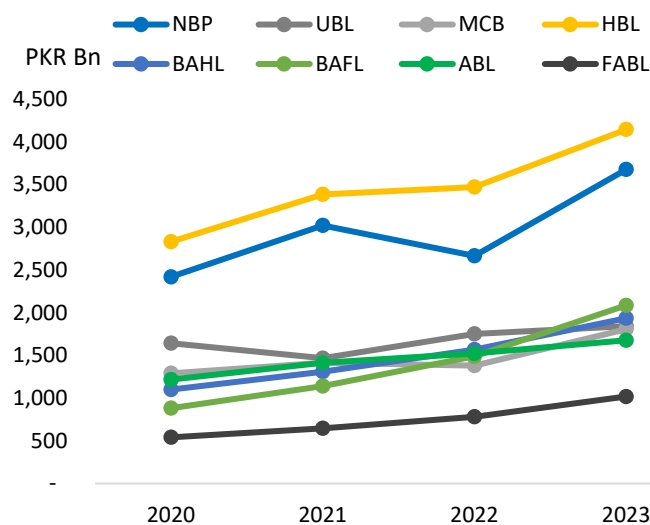
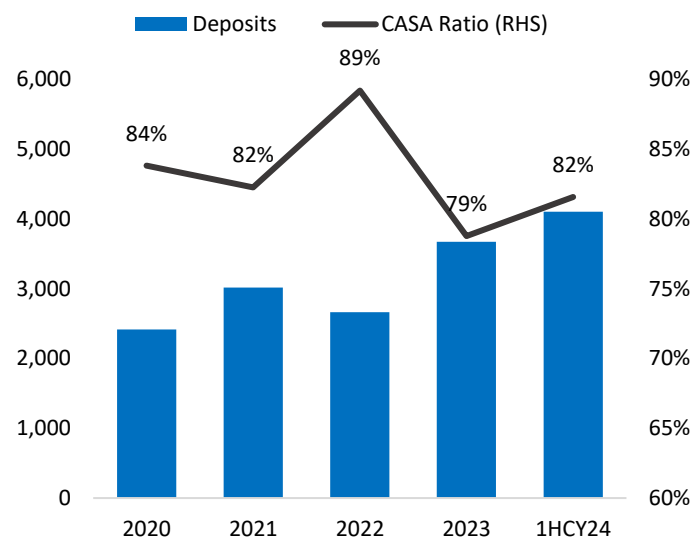


Exhibit: High proportion of CASA in total deposits (PKRbn)

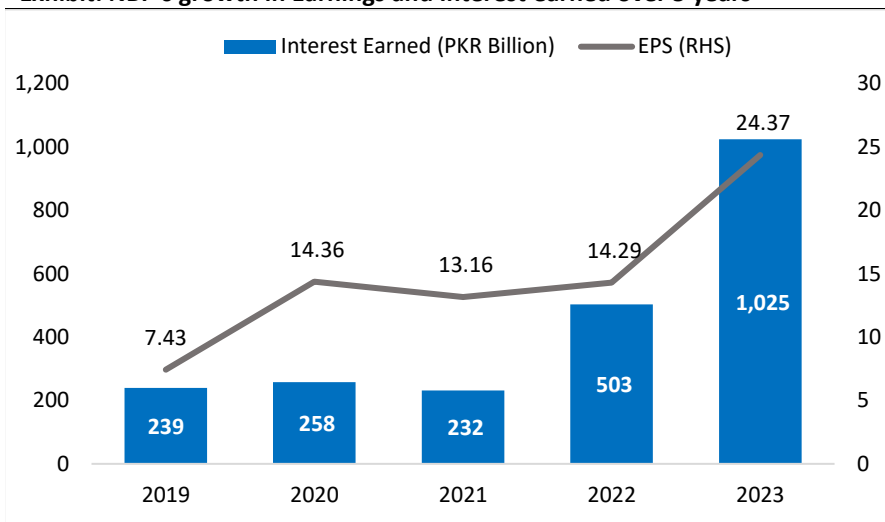


Source: Company Accounts, IGI Research

6. Strong Growth in Earnings

In CY23, the bank registered a robust 70% growth in earnings clocking in at PKR 52bn (EPS: PKR: 24.4/share) whereas in 1HCY24, the bank posted a hefty loss of PKR 10bn (LPS: PKR: 4.92/share) as the bank accounted for the pension payment in this period. The earnings are expected to take a hit in CY24, however it will start to improve CY25 onwards especially with the potential decline in interest rates, the NPLs are projected to drop leading the bank to book provision reversals which will further support earnings. We project earnings to grow at a 5 year CAGR of 24% from CY24-28. Moreover, NBP's Net Interest Margins (NIMs) are expected to shrink in CY25 with the decline in interest rates which the Bank will alleviate by working on building up its earning assets.

Exhibit: NBP's growth in Earnings and Interest earned over 5 years



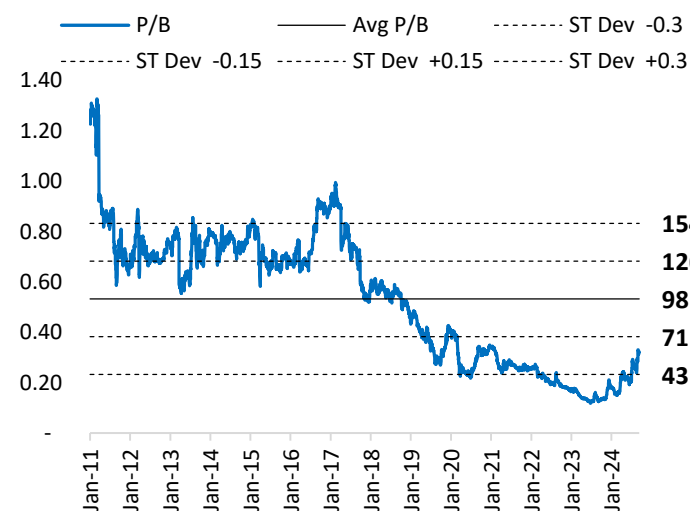
Source: Company Accounts, IGI Research

7. Discounted P/B compared to Peers

NBP is trading at an attractive P/B multiple of 0.33x as compared to the industry average of 0.74x. NBP's P/B has remained lower compared to its historic average due to pension liability case. Since 2017, NBP's P/B has averaged 0.36x compared to average of 0.76x between 2011-2016. With settlement of pension case, we expect NBP's P/B multiple to re-rate to pre 2017 levels and stand in line with industry average.

Exhibit: NBP Historical P/B

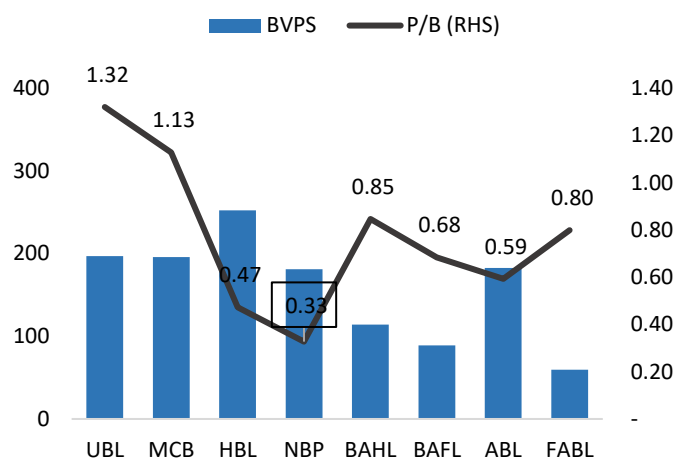
Based on historical average P/B of 0.5x, NBP's value comes at PKR 98/share.



Source: Company Accounts, CapitalStake, IGI Research

Exhibit: P/B Comparison of IGI's Banking Sector Universe

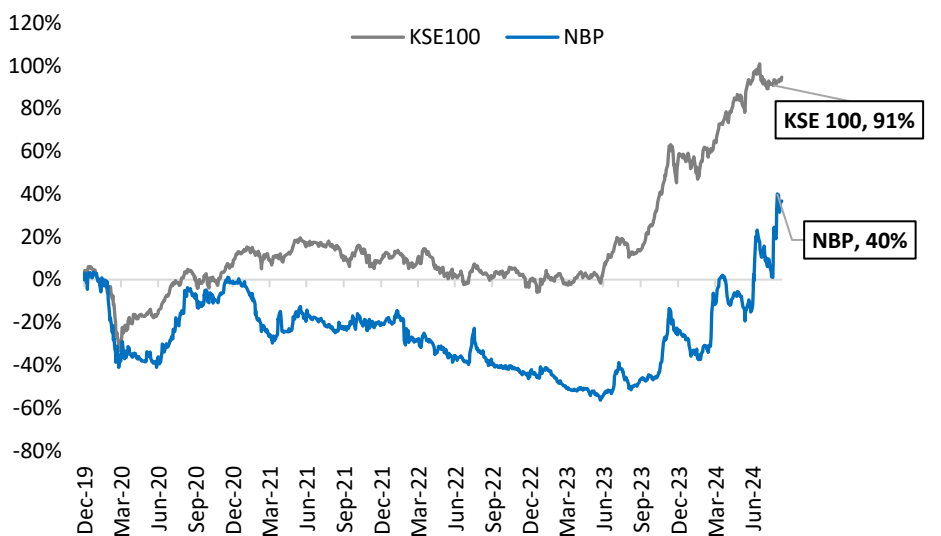
NBP remains one of the cheapest banks in our universe based on P/B



Valuation

We have a 'BUY' rating on NBP with a Jun-25 target price of PKR 82.6/share offering a ~40% upside from the last closing price of PKR 59.2/share (10-Sep-24). We have determined our target price using Justified P/B Ratio methodology with forecasted average ROE of 10.9% (CY24-CY28) and justified P/B multiple of 0.40x.

Exhibit: Relative Price Performance



Source: Company Accounts, CapitalStake, IGI Research

Key Catalysts

1. Increase in Non-Interest Income
2. Accumulation of low cost deposits
3. Growth in private sector borrowings as economy picks up.

Risk to Rating

1. Asset Quality Risks such as increase in Non-performing loans.
2. Implementation of IFRS-9.
3. Imposition of additional tax on ADR below 50%.

Financial Summary

National Bank of Pakistan (NBP)

Current Price (PKR): 59.2 Target Price (PKR): 82.6 Upside: 40% Recommendation: BUY

Period end (Dec) - PKRbn CY20A CY21A CY22A CY23A CY24F CY25F CY26F CY20A CY21A CY22A CY23A CY24F CY25F CY26F

Income Statement								Per Share							
Net Interest Income	104	98	117	169	146	141	162	EPS	14.4	13.2	14.3	24.4	9.7	16.7	21.4
Fee Income	18	18	21	22	30	34	39	DPS	-	1.0	-	-	5.0	8.5	14.0
Non-Interest Income	36	37	37	41	50	55	61	BVPS	125.8	134.5	141.4	179.9	184.6	192.7	200
Total Revenue	140	135	154	209	197	196	223	Ratios							
Operating Expense	63	60	78	94	103	115	121	Profit Margin	22%	21%	20%	25%	11%	18%	20%
Profit Before Tax	46	53	63	101	40	70	89	Cost/Income	45%	45%	51%	45%	52%	59%	55%
Profit After Tax	31	28	30	52	21	35	46	Eff. Tax Rate	34%	47%	52%	49%	49%	49%	49%
Balance Sheet								NIMs	4.3%	3.6%	3.0%	3.2%	2.4%	2.1%	2.2%
Balances with TR Banks	249	279	230	295	396	366	425	Gross ADR	48%	43%	54%	44%	40%	42%	44%
Lending	127	335	31	192	327	262	262	Net IDR	60%	64%	130%	120%	115%	116%	113%
Investments- Net	1,463	1,938	3,477	4,403	4,965	5,559	6,126	Valuation							
Advances- Net	983	1,113	1,231	1,398	1,501	1,749	2,052	P/E	4.1x	4.5x	4.1x	2.4x	6.1x	3.6x	2.8x
Borrowings	139	313	1,940	2,178	2,396	2,635	2,899	DY	0%	2%	0%	0%	8%	14%	24%
Deposits	2,419	3,019	2,666	3,674	4,322	4,787	5,409	P/B	0.5x	0.4x	0.4x	0.3x	0.3x	0.3x	0.3x
Share Capital	21	21	21	21	21	21	21	ROE (%)	11%	10%	10%	15%	6%	9%	12%
Unappropriated Profit	116	140	173	219	229	246	262	ROA (%)	1%	1%	1%	1%	0%	1%	1%
Reserves	57	60	64	79	79	79	79	Non-Financial Information							
Total Equity	268	286	301	383	393	410	426	Branches	1,514	1,513	1,512	1,508	1,508	1,508	1,508

Source: PSX, Capital Stake, Company Accounts, Bloomberg, IGI Research

2QCY24 Financial Performance

NBP announced its 2QCY24 results and reported a loss of PKR 10bn (LPS: PKR 4.92/share) mainly attributable to a one-time extraordinary payment of pension expense amounting to PKR 49bn. During the period, the Bank reported net interest income of PKR 43bn up by 5%y/y and 48%q/q. Moreover, the fee and commission income reported an incline of 8%y/y while the treasury income declined by 8%y/y keeping the non-interest income flat on a y/y basis at PKR 12bn. The total revenue of the bank clocked in at PKR 54bn up by 4%y/y (34%q/q). The operating expense was recorded at PKR 27bn for the period with the cost/income ratio settling at 50% (2QCY23: 44%). The bank recorded a provision charge of PKR 1bn as compared to PKR 0.3bn in the same period last year. The tax charge for this quarter was recorded at PKR 10bn (effective tax rate of 49% compared to 78% in 2QCY23).

Exhibit: NBP Quarterly Financial Highlights - 2QCY24					
PKR Billion	2QCY24	2QCY23	Y/Y	1QCY24	Q/Q
Net Interest Income	43	41	5%	29	48%
Fee Income	6	6	8%	6	16%
Treasury Income	5	6	-8%	5	0%
Non-Interest Income	12	12	0%	12	0%
Total Revenue	54	52	4%	41	34%
Op. Expense	27	23	18%	22	23%
Provision Charge	1	0	310%	1	68%
Profit Before Tax	-21	18	-214%	21	-198%
Tax	-10	14	-172%	10	-197%
Profit after Tax	-10	15	-168%	11	-198%
EPS	-4.92	7.21	-168%	5.04	-93%
DPS	-	-	-	-	-
Cost/Income	50%	44%	6%	54%	69%
Effective tax	49%	78%	-29%	49%	100%

Source: Company Accounts, IGI Research, *Number of shares (bn): 2.13

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Buy if target price on aforementioned security (ies) is more than 10%, from its last closing price(s)

Hold if target price on aforementioned security (ies) is in between -10% and 10%, from its last closing price(s)

Sell if target price on aforementioned security (ies) is less than -10%, from its last closing price(s)

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- Discounted Cash Flow (DCF)
- Reserve Based DCF
- Dividend Discount Model (DDM)
- Justified Price to Book
- Residual Income (RI)
- Relative Valuation (Price to Earning, Price to Sales, Price to Book)

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