

Institutional Equity Research

**Punjab National Bank**

Banking | India

1QFY18 Result Update | August 03, 2017

CMP* (Rs)	159
Upside/ (Downside) (%)	5
Bloomberg Ticker	PNB IN
Market Cap. (Rs bn)	338
Free Float (%)	38
Shares O/S (mn)	2,128

**HOLD** 

Target Price: Rs167

**Credit Cost to Remain Elevated; Reiterate HOLD**

Punjab National Bank (PNB) has delivered a healthy performance in 1QFY18. Its PAT surged by 12.1% YoY and 31.2% QoQ to Rs3.4bn led by lower provisioning expenses (-4.7% YoY & -54.7% QoQ to Rs26.1bn) and higher treasury and exchange income (+47.2% YoY and +0.3% QoQ to Rs10.7bn). Fresh slippages declined to Rs66.5bn in 1QFY18 vs. Rs69bn in 4QFY17 and Rs92.3bn in 1QFY17. On QoQ basis, PNB's loan book dipped by 4.7% owing to 17.8%, 4% and 3.3% QoQ decline in overseas, MSME and large corporate loan book, respectively. However, PNB witnessed 2.9% QoQ and 15.9% YoY growth on retail loan front led by mortgage and auto segments.

**Management Commentary & Guidance**

- ▶ PNB has total exposure of Rs11.0bn towards 9 loans out of 12 loans referred to Insolvency & Bankruptcy Code (IBC) by the RBI. The Bank will need additional provisioning of Rs10bn in next three quarters depending upon development on resolution front.
- ▶ Further, the Bank has exposure of Rs30.4bn towards next 50 stressed accounts and currently having ~50% provisioning converge on these accounts. The Management does not expect any further provisioning requirement for on these accounts.
- ▶ Deliberately lowering its international loan book due to lower profitability, the Bank focuses more on high-yielding retail and other small ticket loans. The Management expects its loan book to grow by 20% in FY18 led by Retail, mid-Corporate and Agri segments.
- ▶ The Bank has taken necessary permission to raise Rs30bn in core equity and expects to complete the transaction by the FY18-end. Further, it is planning to raise Rs10bn through monetisation of non-core assets and subsidiaries.
- ▶ PNB expects NIMs to decline marginally in FY18 led by shifting of loan from base rate to MCLR. However, higher upgrades and recovery may help it to sustain NIMs at current level.

**Outlook & Valuation**

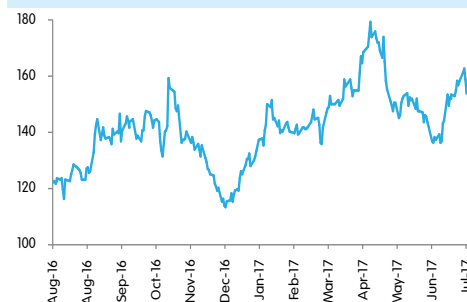
The Government of India is mulling consolidation in PSU banking space and PNB is expected to be one of the anchor bank/acquiring banks. This creates very high level of uncertainty for its future earnings trajectory. Moreover, the stressed asset portfolio of the Bank remains uncomfortable at high level of 16.4%, which is one of the highest among the large PSBs. Further, 2.8% of stressed loans are from standard restructured portfolio on which the Bank holds much lower provisioning coverage. Additionally, its specific PCR on gross NPA portfolio also remains at lower level of 40.1% as of Jun'17. Consequently, we expect PNB's credit cost to remain elevated, which would keep its earnings and return ratio subdued over next 4-6 quarters. **Hence, we reiterate our HOLD recommendation on the stock with an unrevised SOTP-based Target Price of Rs167 (valuing parent at 1x FY19 Adj. BV implying standalone value at of Rs125 and valuing subsidiaries at Rs42 after 15% holding company discount).**

Key Financials (Rs mn)	FY16	FY17	FY18E	FY19E
NII	153,118	149,932	166,558	184,395
PPP	113,394	145,652	152,592	172,410
PAT	(39,744)	13,248	20,192	43,920
EPS (Rs)	(20.2)	6.2	9.5	20.6
P/E (x)	(7.9)	25.5	16.8	7.7
Adj. BV (Rs)	90.4	102.2	105.8	124.6
P/Adj. BV (x)	1.8	1.6	1.5	1.3
Gross NPA (%)	13.5	13.2	13.4	10.9
Net NPA (%)	8.6	7.8	9.5	7.4
Avg. ROA (%)	(0.6)	0.2	0.3	0.5
Avg. ROE (%)	(10.4)	3.2	4.8	9.5

Source: Company, RSec Research

Share price (%)	1 mth	3 mth	12 mth
Absolute performance	15.8	(5.9)	30.0
Relative to Nifty	9.9	(14.2)	13.3

Shareholding Pattern (%)	Mar'17	Jun'17
Promoter	65.0	65.0
Mutual Funds	5.8	5.8
Insurance Companies	13.7	13.3
Foreign Portfolio Investors	10.0	10.4
Others	5.6	5.5
<b>Total</b>	<b>100.0</b>	<b>100.0</b>

**1 Year Stock Price Performance**

Note: \* CMP as on Aug 02, 2017

Research Analyst : Asutosh Kumar Mishra  
 Contact : (022) 33201323  
 Email : asutosh.mishra@relianceada.com

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## Risks to view

- Downside risk to our rating is any material changes on asset quality front.
- Upside risk to our rating is faster-than-expected business growth.

## Exhibit 1: Income Statement Analysis

(Rs mn)	1Q FY18	1Q FY17	% yoy / bps	4Q FY17	% qoq / bps	FY 2017	FY 2016	% yoy / bps
Interest on Advance	81,448	85,099	(4.3)	77,187	5.5	329,588	344,455	(4.3)
YoA - Calculated (%)	8.0	8.5	(52)	7.7	28	7.9	8.7	(76)
Income on Investment	34,036	27,852	22.2	35,105	(3.0)	125,772	120,337	4.5
Interest on Balances	5,513	2,357	133.9	5,663	(2.6)	13,542	7,305	85.4
Others Interests	366	442	(17.2)	909	(59.8)	3,858	2,147	79.7
<b>Interest Earned</b>	<b>121,364</b>	<b>115,749</b>	<b>4.9</b>	<b>118,865</b>	<b>2.1</b>	<b>472,760</b>	<b>474,244</b>	<b>(0.3)</b>
Interest Expended	82,812	78,759	5.1	82,030	1.0	322,828	321,126	0.5
CoF - Calculated (%)	4.7	4.9	(22)	4.7	1	4.8	5.2	(43)
<b>Net Interest Income</b>	<b>38,551</b>	<b>36,990</b>	<b>4.2</b>	<b>36,835</b>	<b>4.7</b>	<b>149,932</b>	<b>153,118</b>	<b>(2.1)</b>
NIM - Calculated (%)	2.3	2.4	(13)	2.2	9	2.3	2.6	(25)
NIM - Reported (%)	3.5	2.5	109	2.8	79	2.4	2.6	(22)
NII as % of Oper. Income	62.3	61.1	121	54.3	803	62.6	71.8	(923)
Core Fee Income	13,400	10,220	31.1	11,120	20.5	40,890	34,700	17.8
Fee Inc. as % of OI	21.7	16.9	478	16.4	527	17.1	16.3	5
Non Core Fee Income	9,918	13,331	(25.6)	19,908	(50.2)	48,624	25,301	92.2
Non core fee Inc. as % of OI	16.0	22.0	(599)	29.3	(1,331)	20.3	11.9	71
<b>Total Other Income</b>	<b>23,318</b>	<b>23,551</b>	<b>(1.0)</b>	<b>31,028</b>	<b>(24.8)</b>	<b>89,514</b>	<b>60,001</b>	<b>49.2</b>
Other Inc. as % of OI	37.7	38.9	(121)	45.7	(803)	37.4	28.2	923
<b>Operating Income (OI)</b>	<b>61,869</b>	<b>60,541</b>	<b>2.2</b>	<b>67,863</b>	<b>(8.8)</b>	<b>239,445</b>	<b>213,118</b>	<b>12.4</b>
Core Operating Income	51,951	47,210	10.0	47,955	8.3	190,822	187,818	1.6
Employees Expenses	19,373	18,998	2.0	(5,484)	(453.3)	54,207	64,260	(15.6)
Employees Expn. as % of OI	31.3	31.4	(7)	(8.1)	3,939	22.6	30.2	(751)
Other Operating Expenses	10,323	8,797	17.4	11,029	(6.4)	39,587	35,465	11.6
Other Oper Exp. as % of OI	16.7	14.5	216	16.3	43	16.5	16.6	(11)
<b>Total Operating Expenses</b>	<b>29,696</b>	<b>27,794</b>	<b>6.8</b>	<b>5,545</b>	<b>435.5</b>	<b>93,794</b>	<b>99,725</b>	<b>(5.9)</b>
Cost to income Ratio (%)	48.0	45.9	209	8.2	3,983	39.2	46.8	(762)
<b>Operating Profit (OP)</b>	<b>32,173</b>	<b>32,746</b>	<b>(1.8)</b>	<b>62,318</b>	<b>(48.4)</b>	<b>145,652</b>	<b>113,394</b>	<b>28.4</b>
Provisions and Conting.	26,087	27,384	(4.7)	57,535	(54.7)	125,536	170,773	(26.5)
Pro Burden as % of OP	81.1	83.6	(254)	92.3	(1,124)	86.2	150.6	(6,441)
<b>Profit Before Tax</b>	<b>6,086</b>	<b>5,362</b>	<b>13.5</b>	<b>4,783</b>	<b>27.2</b>	<b>20,115</b>	<b>(57,379)</b>	<b>(135.1)</b>
Tax Expenses	2,652	2,299	15.4	2,164	22.6	6,867	(17,635)	(138.9)
Effective Tax Rate (%)	43.6	42.9	71	45.2	(167)	34.1	30.7	341
<b>Net Profit</b>	<b>3,434</b>	<b>3,064</b>	<b>12.1</b>	<b>2,619</b>	<b>31.1</b>	<b>13,248</b>	<b>(39,744)</b>	<b>(133.3)</b>
EPS	1.6	1.6	3.2	1.2	30.9	6.5	(20.8)	(131.0)

Source: Company, RSec Research

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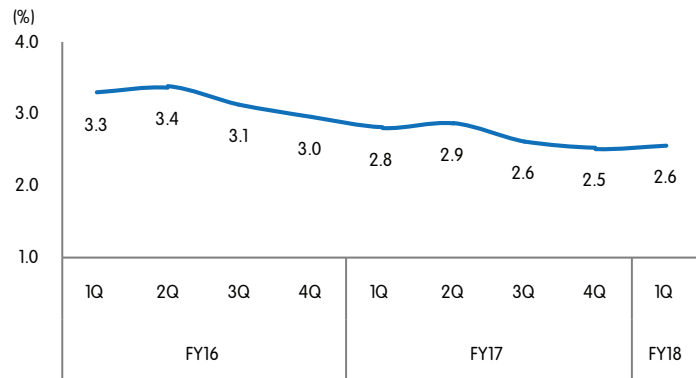
# Punjab National Bank

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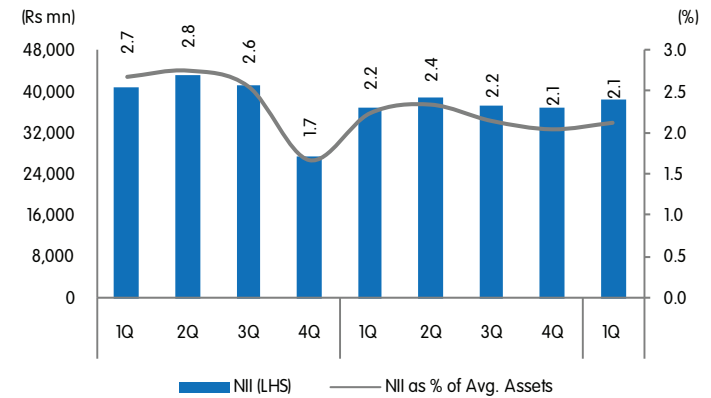
CMP* (Rs)	159
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**HOLD** 

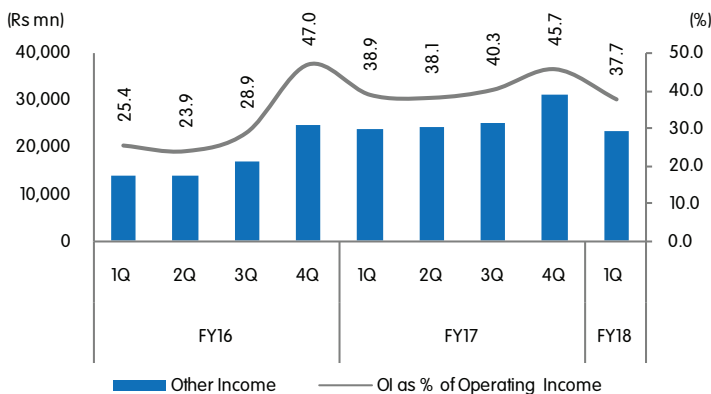
Target Price: Rs167

**Exhibit 2: Domestic NIMs improved by 5bps QoQ led by 15bps QoQ rise in yield on loan**


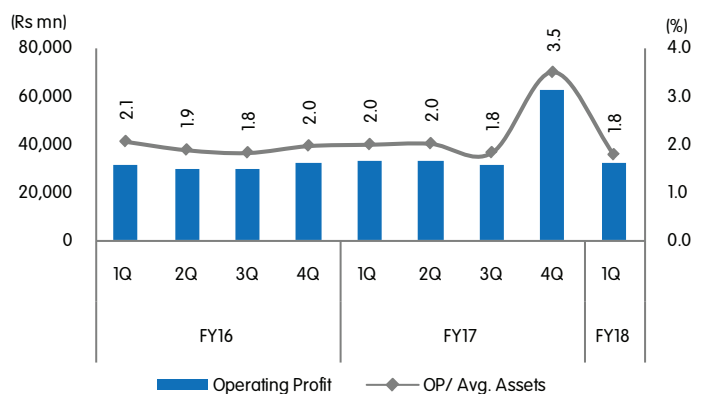
Source: Company, RSec Research

**Exhibit 3: NII growth remained muted owing to lower growth in loan book**


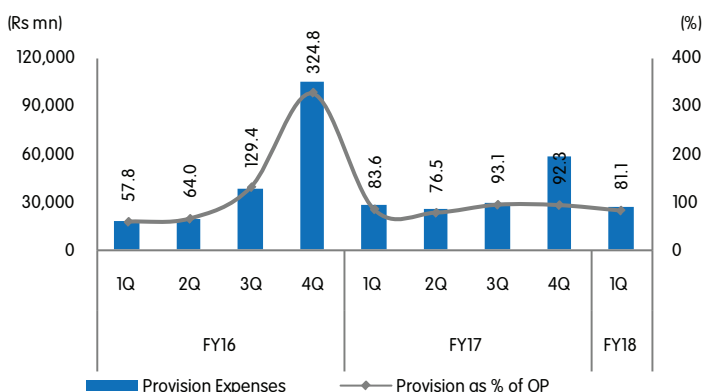
Source: Company, RSec Research

**Exhibit 4: Other income growth declined sequentially due to lower recovery from W/O accounts**


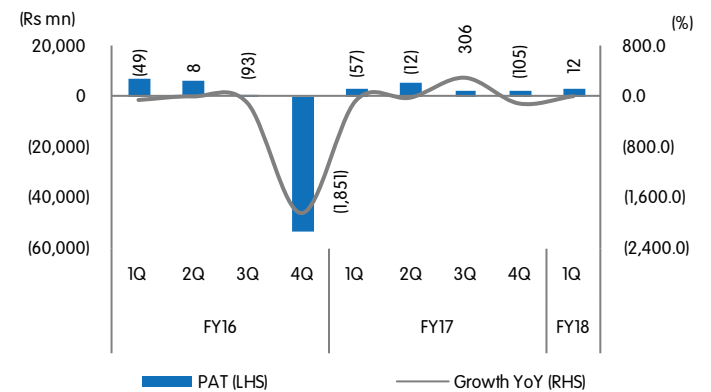
Source: Company, RSec Research

**Exhibit 5: Overall operating profit growth remained subdued led by sequential increase in opex**


Source: Company, RSec Research

**Exhibit 6: Provisioning expenses declined sequentially due to moderation in fresh slippages**


Source: Company, RSec Research

**Exhibit 7: PAT growth was led by lower provisioning expenses and higher Treasury & Exchange income**


Source: Company, RSec Research

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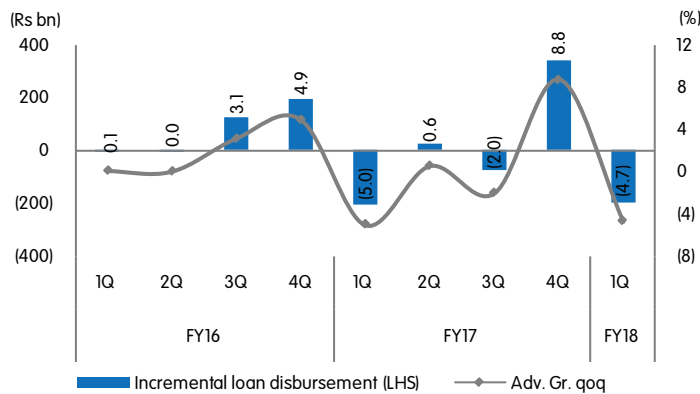
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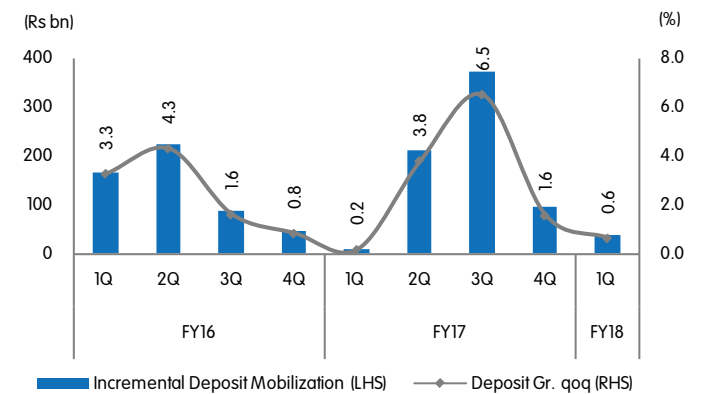
**Exhibit 8: Balance Sheet Analysis**

(Rs bn)	4Q FY16	1Q FY17	2Q FY17	3Q FY17	4Q FY17	1Q FY18	QoQ% / bps	YoY % / bps
Net Worth	383.1	395.7	422.2	424.1	418.5	425.2	1.6	7.5
Deposit	5,531	5,540	5,749	6,122	6,217	6,256	0.6	12.9
Savings Deposits	1,694	1,711	1,801	2,220	2,142	2,115	(1.2)	23.6
Current Deposits	362	324	361	408	459	400	(12.7)	23.5
CASA Deposit	2,056	2,035	2,162	2,628	2,600	2,516	(3.3)	23.6
Term Deposit	3,475	3,504	3,587	3,494	3,617	3,741	3.4	6.7
Investments	1,578	1,492	1,715	2,218	1,867	2,025	8.5	35.8
Advances	4,123	3,916	3,937	3,857	4,195	3,997	(4.7)	2.1
Total Business	11,232	10,947	11,401	12,197	12,279	12,279	(0.0)	12.2
Avg Int. Earning Assets	4,258	6,039	6,183	6,405	5,358	4,356	(18.7)	(27.9)
Risk Weighted Assets (Rs mn)	4,249	4,212	4,392	4,404	4,556	4,547	(0.2)	8.0
CAR (%)	11.3	11.6	11.7	11.6	11.7	11.6	(2)	6
Tier I Capital (%)	8.4	8.6	8.8	8.3	8.9	8.9	3	32

Source: Company, RSec Research

**Exhibit 9: Loan book growth remained subdued due to sequential decline in international, MSME and large corporate loan book**


Source: Company, RSec Research

**Exhibit 10: Deposit de-grew due to increased drawdown of CASA deposits post demonetization**


Source: Company, RSec Research

**Exhibit 11: Loan Book Analysis**

(Rs mn)	4Q FY16	1Q FY17	2Q FY17	3Q FY17	4Q FY17	1Q FY18	QoQ%	YoY %
Agriculture	626,040	613,940	635,110	617,090	669,310	656,110	(2.0)	6.9
SME/MSME	803,540	782,690	865,540	789,330	815,920	783,530	(4.0)	0.1
Large Industry	1,231,800	1,203,110	1,123,320	1,136,120	1,255,790	1,213,910	(3.3)	0.9
Retail	578,010	585,500	614,220	610,350	659,820	678,670	2.9	15.9
Others (Incl. NBFC)	559,100	390,700	370,650	409,080	516,660	481,070	(6.9)	23.1
Overseas	529,260	544,480	533,220	498,450	500,010	411,230	(17.8)	(24.5)

Source: Company, RSec Research

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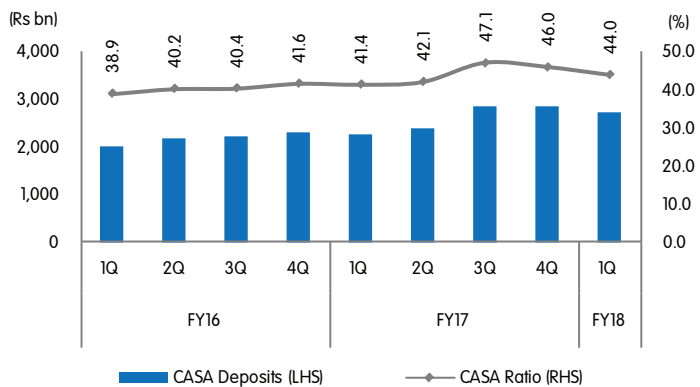
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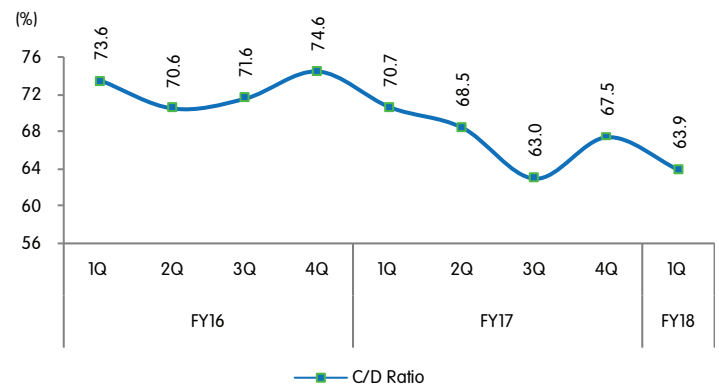
**Exhibit 12: Loan Book Analysis (% Break Up)**

	4Q FY16	1Q FY17	2Q FY17	3Q FY17	4Q FY17	1Q FY18	QoQ bps	YoY bps
Agriculture	14.5	14.9	15.3	15.2	15.2	15.5	38	63
SME/MSME	18.6	19.0	20.9	19.4	18.5	18.5	8	(45)
Large Industry	28.5	29.2	27.1	28.0	28.4	28.7	31	(46)
Retail	13.4	14.2	14.8	15.0	14.9	16.1	113	186
Others (Incl. NBFC)	12.9	9.5	8.9	10.1	11.7	11.4	(31)	191
Overseas	12.2	13.2	12.9	12.3	11.3	9.7	(158)	(348)

Source: Company, RSec Research

**Exhibit 13: As a result, CASA ratio declined to 44% in 1QFY18 from all-time high of 46%**


Source: Company, RSec Research

**Exhibit 14: C/D ratio of the Bank remained at relatively lower level**


Source: Company, RSec Research

**Exhibit 15: Asset Quality Analysis**

(Rs mn)	4Q FY16	1Q FY17	2Q FY17	3Q FY17	4Q FY17	1Q FY18	QoQ% / bps	YoY % / bps
Gross Non Performing Assets	558,183	566,541	564,656	556,275	553,705	577,207	4.2	1.9
Fresh Slippages	235,448	92,280	62,020	56,600	68,960	66,490	(3.6)	(27.9)
Net Non Performing Assets	354,226	357,285	357,223	349,935	327,021	345,727	5.7	(3.2)
GNP Ratio (%)	12.9	13.7	13.6	13.7	13.2	13.7	46	(8)
NNP Ratio (%)	8.6	9.2	9.1	9.1	7.8	8.7	87	(49)
NPA Coverage Ratio	36.54	36.94	36.74	37.09	40.94	40.10	(84)	317
Restructured Gross Loans	201,440	189,090	180,940	172,160	119,320	110,510	(7.4)	(41.6)
Restructured Loan as % of Adv.	4.9	4.8	4.6	4.5	2.8	2.8	(8)	(206)

Source: Company, RSec Research

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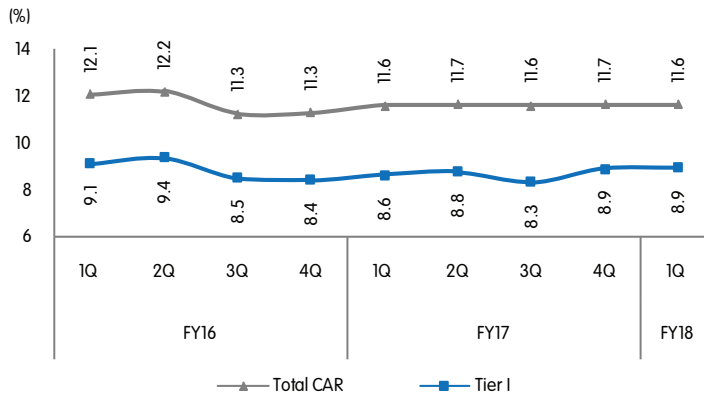
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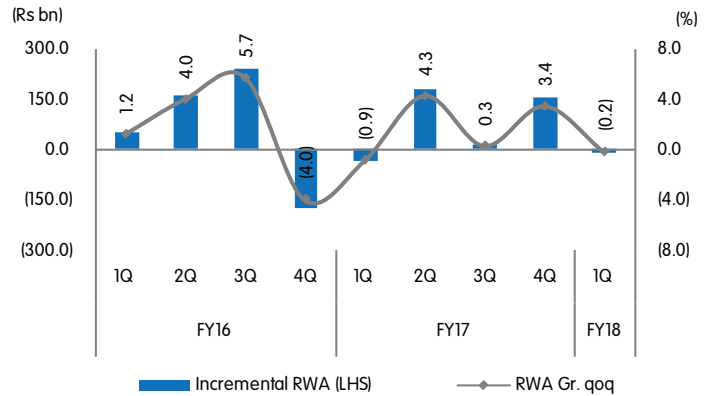
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**Exhibit 16: GoI funding and utilisation of additional limit in AT-1 and Tier-II bonds will support PNB's growth plan**



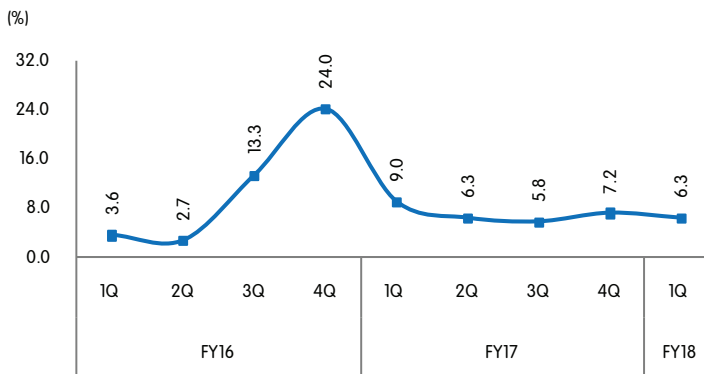
Source: Company, RSec Research

**Exhibit 17: Bank continues to focus on the segments having relatively lower risk weight**



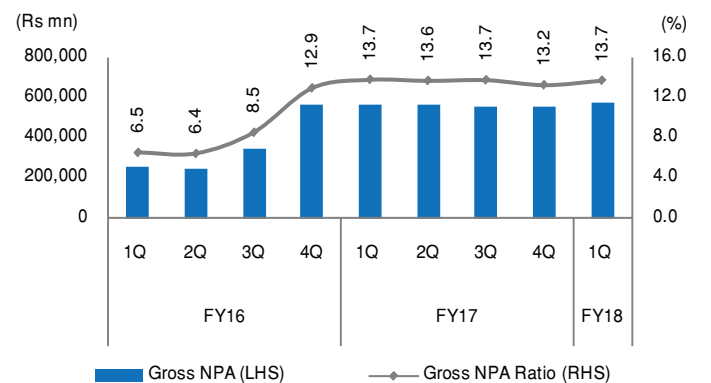
Source: Company, RSec Research

**Exhibit 18: Fresh slippages primarily came from large corporate segments**



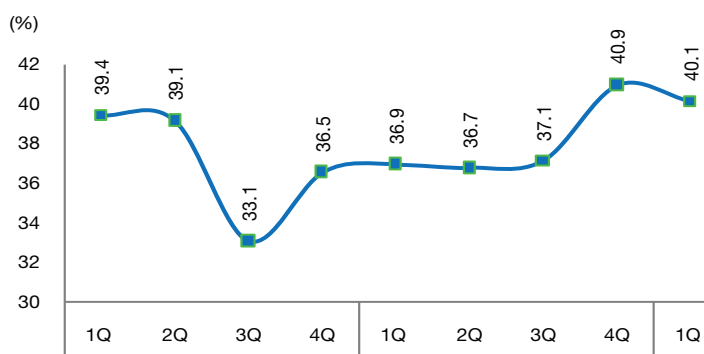
Source: Company, RSec Research

**Exhibit 19: Elevated fresh slippages continued to impact asset quality negatively**



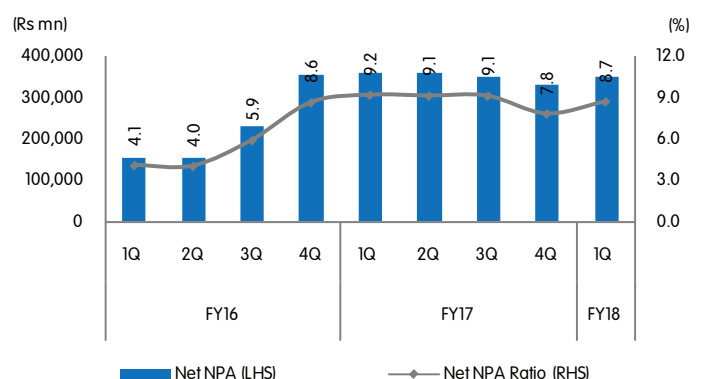
Source: Company, RSec Research

**Exhibit 20: PCR declined due to relatively lower provisioning during the quarter**



Source: Company, RSec Research

**Exhibit 21: Higher GNP formation and lower provisioning expenses led to sharp rise in net NPA**



Source: Company, RSec Research

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## Profit & Loss Statement

Y/E March (Rs mn)	FY16	FY17	FY18E	FY19E
Interest Earned	474,244	472,760	493,892	532,035
Interest Expenditure	321,126	322,828	327,334	347,641
<b>Net Interest Income</b>	<b>153,118</b>	<b>149,932</b>	<b>166,558</b>	<b>184,395</b>
Fee Income	27,874	32,279	39,846	47,706
Non Fee Income	32,127	57,235	52,907	58,230
<b>Other Income</b>	<b>60,001</b>	<b>89,514</b>	<b>92,753</b>	<b>105,936</b>
Net Operating Income	213,118	239,445	259,310	290,330
<b>Core Operating Income</b>	<b>180,991</b>	<b>182,210</b>	<b>206,403</b>	<b>232,101</b>
Employee Expenses	64,260	54,207	63,964	71,960
Other Expenses	35,465	39,587	42,754	45,960
Operating Expenses	99,725	93,794	106,718	117,920
<b>Operating Profit</b>	<b>113,394</b>	<b>145,652</b>	<b>152,592</b>	<b>172,410</b>
Provisions and Contingencies	170,773	125,536	121,765	106,858
<b>Profit Before Tax</b>	<b>(57,379)</b>	<b>20,115</b>	<b>30,828</b>	<b>65,552</b>
Taxes	(17,635)	6,867	10,635	21,632
<b>Profit After Tax</b>	<b>(39,744)</b>	<b>13,248</b>	<b>20,192</b>	<b>43,920</b>

## Balance Sheet

Y/E March (Rs mn)	FY16	FY17	FY18E	FY19E
<b>Capital &amp; Liabilities</b>				
Capital	3,927	4,256	4,256	4,256
Reserves Total	379,174	414,214	415,988	457,167
<b>Net Worth</b>	<b>383,101</b>	<b>418,470</b>	<b>420,244</b>	<b>461,423</b>
<b>Deposits</b>	<b>5,530,511</b>	<b>6,217,040</b>	<b>6,807,659</b>	<b>7,556,502</b>
Current deposits	361,570	458,533	449,305	498,729
Saving deposits	1,694,264	2,141,626	2,409,911	2,693,893
Term Deposits	3,474,678	3,616,882	3,948,442	4,363,880
Borrowings	597,552	407,633	428,633	450,683
Other Liabilities & Provisions	162,740	160,162	162,854	179,428
<b>Total Liabilities</b>	<b>6,673,905</b>	<b>7,203,306</b>	<b>7,819,391</b>	<b>8,648,036</b>
<b>Assets</b>				
Cash & Cash Equivalents	756,231	883,317	802,482	844,465
Investments	1,578,459	1,867,254	2,085,052	2,275,218
Advances	4,123,258	4,194,932	4,656,374	5,238,421
Fixed Assets	52,227	62,733	68,708	71,785
Other Assets	163,729	195,071	206,775	218,148
<b>Total Assets</b>	<b>6,673,905</b>	<b>7,203,306</b>	<b>7,819,391</b>	<b>8,648,036</b>

## Institutional Equity Research

## Punjab National Bank

Banking | India

CMP* (Rs)	159
Upside/ (Downside) (%)	5
Bloomberg Ticker	PNB IN

**HOLD** 

Target Price: Rs167

## Per Share Data and Valuation

Y/E March	FY16	FY17	FY18E	FY19E
No. of Shares (Mn)	1,963.6	2,128.0	2,128.0	2,128.0
Earnings Per Share (Rs.)	(20.2)	6.2	9.5	20.6
Book Value / Share (Rs.)	180.6	179.0	187.0	205.9
ABV/Share (Rs.)	90.4	102.2	105.8	124.6
Dividend Per Share (Rs.)	-	-	1.3	1.5
Price/ Earnings (X)	(7.9)	25.5	16.8	7.7
Price/ BV (X)	0.9	0.9	0.9	0.8
Price/Adjusted BV (X)	1.8	1.6	1.5	1.3

## Key Assumptions

Y/E March (%)	FY16	FY17	FY18E	FY19E
Loan Growth	8.4	1.7	11.0	12.5
Deposit Growth	10.3	12.4	9.5	11.0
RWA Growth	6.9	7.2	15.2	11.4
Slippages Ratio	11.1	5.4	5.0	3.5
Cost of Fund	5.2	4.8	4.5	4.3
Yield on Fund	8.0	7.3	7.1	6.9
NIM	2.6	2.3	2.4	2.4
Other Income Growth	1.9	49.2	3.6	14.2
Cost to Income Ratio	46.8	39.2	41.2	40.6
Average Credit Cost	4.7	3.0	2.9	2.3
Effective Tax Rate	30.7	34.1	34.5	33.0

## Growth Rate

Y/E March (%)	FY16	FY17	FY18E	FY19E
Net interest Income	(7.5)	(2.1)	11.1	10.7
Other Income	1.9	49.2	3.6	14.2
Operating Profit	(5.1)	28.4	4.8	13.0
Provisions Expense	113.5	(26.5)	(3.0)	(12.2)
PAT	(229.8)	(133.3)	52.4	117.5
Risk Weighted Assets	6.9	7.2	15.2	11.4

## Yields / Margins

Y/E March (%)	FY16	FY17	FY18E	FY19E
Cost of Funds (CoF)	5.2	4.8	4.5	4.3
Yield on Advance	8.7	7.9	7.6	7.3
Yield on funds	8.0	7.3	7.1	6.9
Net Interest Margin (NIM)	2.6	2.3	2.4	2.4



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## Balance Sheet Ratio

Y/E March (%)	FY16	FY17	FY18E	FY19E
Credit / Deposit Ratio	74.6	67.5	68.4	69.3
Incremental C/D Ratio	61.5	10.4	78.1	77.7
Investment-Deposit Ratio	28.5	30.0	30.6	30.1
CASA Ratio	37.2	41.8	42.0	42.3

## Asset Quality

Y/E March (%)	FY16	FY17	FY18E	FY19E
Gross NPA/Gross Advances	13.5	13.2	13.4	10.9
Net NPA/Net Advances	8.6	7.8	9.5	7.4
Provisioning Burden as % of PPP	150.6	86.2	79.8	62.0
Provisioning Coverage Ratio	36.5	40.9	29.5	31.7
Slippage ratio (%)	11.1	5.4	5.0	3.5
Provis. Exp. to Avg. Advance (%)	4.3	3.0	2.8	2.2

## RoA Tree Analysis

Y/E March (%)	FY16	FY17	FY18E	FY19E
NII / Avg. Assets	2.4	2.2	2.2	2.2
Core Fee / Avg. Assets	0.4	0.5	0.5	0.6
Core Rev. / Avg. Assets	2.8	2.6	2.7	2.8
Ope. Exp. / Avg. Assets	1.6	1.4	1.4	1.4
Cost to Income	46.8	39.2	41.2	40.6
Emp. cost / Avg. Assets	1.0	0.8	0.9	0.9
Oprt. Exp. / Avg. Assets	0.6	0.6	0.6	0.6
Core OP/ Avg. Assets	1.3	1.3	1.3	1.4
Trading & Ot/ Avg. Assets	0.5	0.8	0.7	0.7
OP/ Avg. Assets	1.8	2.1	2.0	2.1
Provisions / Avg. Assets	2.8	1.8	1.6	1.3
NPA prov. / Avg. Assets	2.9	1.8	1.5	1.2
PBT / Avg. Assets	(0.9)	0.3	0.4	0.8
Tax / Avg. Assets	(0.3)	0.1	0.1	0.3
Effective Tax Rate	30.7	34.1	34.5	33.0
RoA	(0.6)	0.2	0.3	0.5
Leverage (x)	17.4	17.2	18.6	18.7
RoE	(10.4)	3.2	4.8	9.5

## Capital Adequacy Ratio

Y/E March (%)	FY16	FY17	FY18E	FY19E
Total CAR	11.3	11.7	11.1	10.5
Tier 1	8.4	8.9	8.5	8.1

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## Rating Guides

Rating	Expected absolute returns (%) over 12 months
BUY	>10%
HOLD	-5% to 10%
REDUCE	>-5%

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