

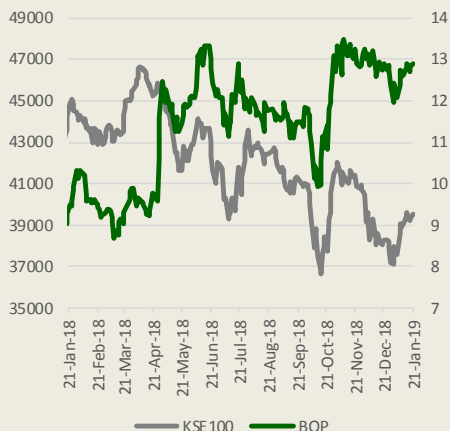
	Call
Buy	Hold
	Sell

KEY STATISTICS

Symbol	BOP
Current Price (Rs)	13.16
Target Price Dec-19 (Rs)	17.50
Market Cap (Rs. mn)	34,791
52 weeks High	13.48
52 weeks Low	8.6
Shares Outstanding (mn)	2,643.69
Free Float (mn)	42%

Source: PSX, Darson Research

RELATIVE PERFORMANCE



KEY STATISTICS

	CY17A	CY18E	CY19E
EPS (Rs)	-1.25	2.73	3.46
P/E (x)	-10.49	4.83	3.80
BVPS (Rs)	11.29	13.98	17.60
P/B (x)	1.17	0.94	0.75
ROE (Tier-I)	-12.3%	21.0%	21.0%

Source: Co. Financials, Darson Research

Research Analyst: Yousuf Saeed
yousuf.saeed@darsononline.com
 +92-21-32467224 Ext: 125

BOP- Initiation of Coverage with a BUY Call

We initiate our coverage on Bank of Punjab (BOP) with a BUY call and Dec-19 TP of Rs17.5/share providing potential upside of 32% from last closing price. Our liking on the stock is based on improved assets quality, impressive deposit growth with focus on low cost deposit, favorable investment mix and enticing valuation. However any increase in provision charges may impact our valuation. The stock is currently trading at CY19E P/E and P/B of 3.8x and 0.75x respectively.

Advances Growth Outperform the Industry Growth

BOP advances grew at the 5 year CAGR of 14.62% as compared to industry 5 year CAGR of ~11%. In 9M CY18 BOP advances posted a growth of ~25% YTD against the industry advances growth of 14.73% in same period. We expect in CY18 bank advances to increase by 28% YoY. Infection ratio of bank moved from 32.76% in CY13 to 12% as of Sep-18 while on the other hand coverage ratio moved to 89% in Sep-18 as compared to 42.78% in CY13 which is inline with industry average of around 88%.

Focus on low cost deposit

BOP's focus on low cost deposit resulted in improved CASA which moved to 71.73% in CY17 as compared to 58.23% in CY12 as a result deposit cost decline from 7.45% in CY12 to 3.07% in CY17. We forecast that CASA may further improve and reach at 74% till CY23.

Bank holds 92% of its Investment in T-Bills

BOP currently holds 92% of its investment in T-Bills which is the highest in our banking universe (avg. of 57%), this places the bank in a well positioned scenario to quickly re-price its investment base with the increase in yield on Government Papers.

CAR stand above the required level

BOP CAR stood at around 13.29% as of Sep-18, after hefty provision during the last decade it was the first time in CY17 (after full provision charged) that the bank is able to meet its CAR required level. In 2008 after loan scandal, BOP CAR ratio declined from 9.78% in CY07 to 1.92% in CY08. Time to time equity injection of Rs23bn further with Rs8.8bn in the form of issuance of TFC and subordinated loan and improved profitability, helped bank to meet the required CAR level.

Enticing Valuation

BOP is currently trading at CY18E/19E P/E and P/B of 4.83/3.8x and 0.94/0.75x. We have a BUY call on the stock with Dec-19 TP of Rs17.5/- based on justified P/B, providing potential upside of 33% from last day closing.

Key Risks

- Higher than estimated provision on NPL
- Lower than estimated deposit growth and change in deposit mix
- Change in regulatory requirements/implementation of IFRS 9

**Vision**

To be customer focused bank with service excellence

Mission

To exceed the expectation of our stakeholders by leveraging our relationship with the Govt. of Punjab and delivering a complete range of professional solutions with a focus on programme driven products and services in the agriculture and middle tier markets through a motivated team.

Rating

PACRA Ratings: AA Long Term and A1+ Short Term.

About the Bank

Bank of Punjab (BOP) is the 10th largest bank of Pakistan. Its head quarter is located in Lahore at BOP Tower. BOP operates with 560 branches (490 conventional and 73 Islamic banking branches) with deposit share of ~4.36% as of Sep-18 in overall industry deposit and a deposit base of Rs568bn.

Government of Punjab holds the major shareholding of the bank with 57.47% holding while the individuals, joint stock companies and others hold 21.46%, 8.02% and 13.05% holding respectively.

The Government of Punjab supported bank by frequently injecting equity, especially after 2008 when few business groups defaulted on their loans. With the efforts of the Punjab Government and its management, bank's profitability turned around and assets' quality improved gradually.

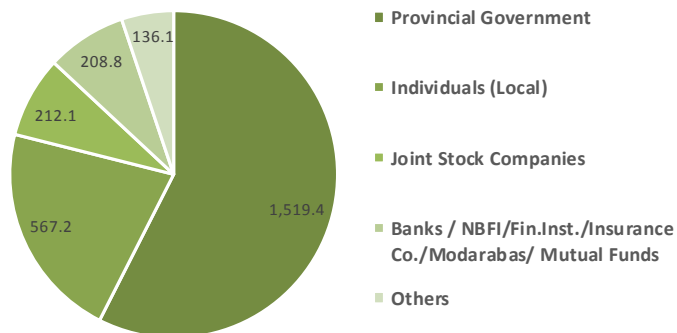
Subsidiary Companies**% of holding**

• Punjab Modarba Service (Pvt.) Ltd.	100.00%
• First Punjab Modaraba	39.16%
• Punjab Capital Securities (Pvt.) Ltd.	39.16%

Categories of Shareholders:**Fig. 1 and 2 Categories of Shareholders**

Categories of Shareholders	No. of Shares (mn)	Percentage%
Provincial Government	1,519.4	57.47%
Individuals (Local)	567.2	21.46%
Joint Stock Companies	212.1	8.02%
Banks / NBFI/Fin.Inst./Insur	208.8	7.90%
Others	136.1	5.15%

Source: Co. Financials, Darson Research



Source: Co. Financials, Darson Research

What went wrong with BOP?

In 2008, non performing loans of the BOP increased from Rs3.34bn in 2007 to Rs.42.68bn in 2008 (Infection ratio 2.45% to 28%) due to aggressive lending of Rs52bn by the management of that time to few business groups with lacked due diligence and proper homework. Furthermore financial crises of 2008 also impacted the overall asset quality due to economic slowdown and higher inflation rate. Bank made provision charge of Rs19bn in its 2008 P&L which affected the overall capital requirement ratios and dampened the interest income of bank.

In 2009 to 2011 Government of Punjab (GoPb) being the major shareholder came to rescue bank and deposited Rs7bn in addition to Rs10bn in CY09 as advance for share subscription money to support the capital requirement. BOP charged further Rs9bn of provision in 2009 and take relaxation from SBP of Rs21bn provision charge due to GoPb support. GoPb issued two Letter of Comfort (LOCs) that in case BOP unable to meet its capital requirement GoPb on behalf of the bank will inject necessary amount of capital to ensure that bank remain compliant with SBP requirements.

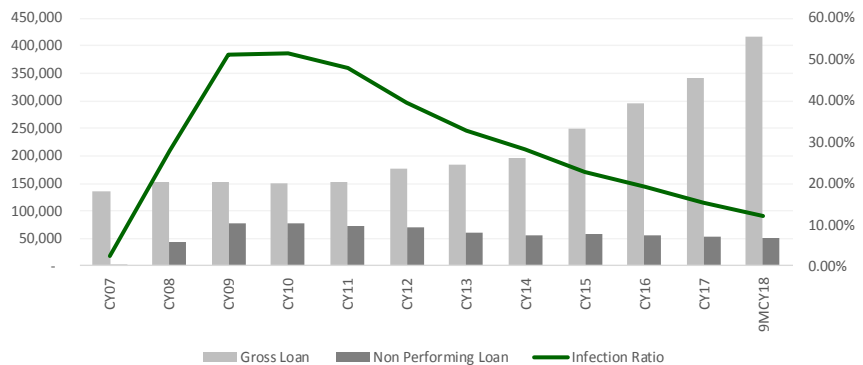
During the year 2013, in first phase, the bank issued Right Shares of Rs5bn. Subsequently, in the second phase, the bank issued right issue of Rs5bn during year 2014. During the year 2014, GoPb also extended a subordinated loan of Rs2bn to support capital structure of the Bank.

In 2016 bank was required by SBP to record provisioning in staggered manner against exposure cover under LOCs aggregating to 15% by Dec-16, 25% by Dec-17 and the remaining by Dec-18. However in CY17 BOP charged the full provision before the expiry date set by the SBP.

Year	Description	Rs. in Bn
CY08	Provision Charge	18.80
CY09	Provision Charge	9.50
CY09	Share Deposit Money I from GoPb	10.00
CY11	Share Deposit Money II from GoPb	7.00
CY13	Issue share of Rs5bn to GoPB	-
CY14	Issue share of Rs5bn to GoPB	-
CY14	Subordinated Loan from GoPb	2.00
CY15	Provision Charge	3.40
CY16	Issue TFC	2.50
CY17	Provision Charge	14.10
CY17	Issue Right Share	5.00

Source: Co Financials, Darson Research

Fig. 3 Gross and Non-Performing Loans (Rs. in Mn)

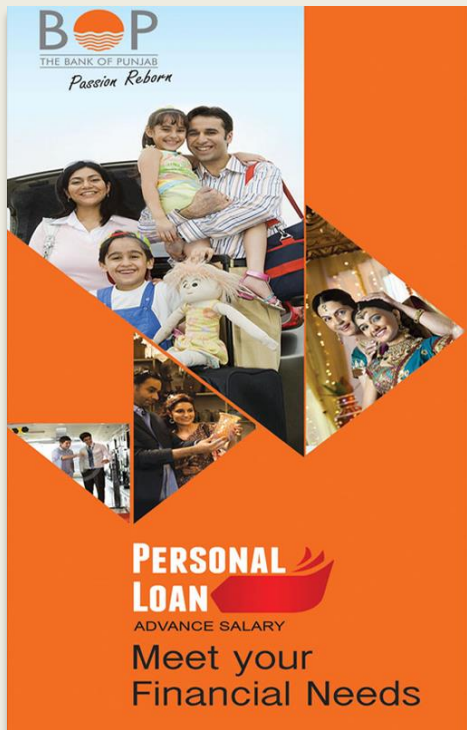


Source: Co. Financials, Darson Research

Advances Growth Outperform the Industry Growth

BOP advances grew at the 5 year CAGR of 14.62% as compared to industry 5 year CAGR of ~11%. In 9M/CY18 BOP advances posted the growth of ~25% YTD against the industry advances growth of 15% in same period. We expect that in CY18 bank advance may increase by 28% YoY.

Restructuring of bank along with effective risk management, BOP assets quality showed the tremendous improvement in last 5 years. Infection ratio of bank moved from 32.76% in CY13 to 12% as of Sep-18 while on the other hand coverage ratio moved to 89% in Sep-18 as compared to 42.78% in CY13 which is inline with industry average of around 88%.

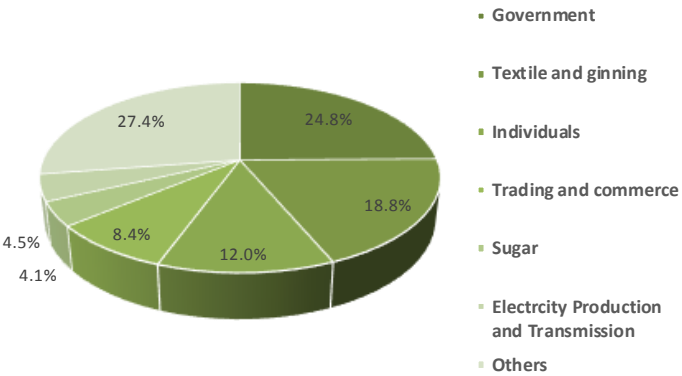


Around 25% of BOP advances are categorized in PSEs and Federal & Provincial Government which are government backed while other major contributors in advances are the textile sector (19%), individuals (12%) and trading companies (8.4%) in total advances of BOP as of CY17.

Textile sector contributes around Rs25bn (48% of total non-performing loans) in non-performing loan on which management has already charged the 85% provision. With Govt's focus to revive textile sector and relief to the export oriented industry, we can't rule out the reversal in provision charges.

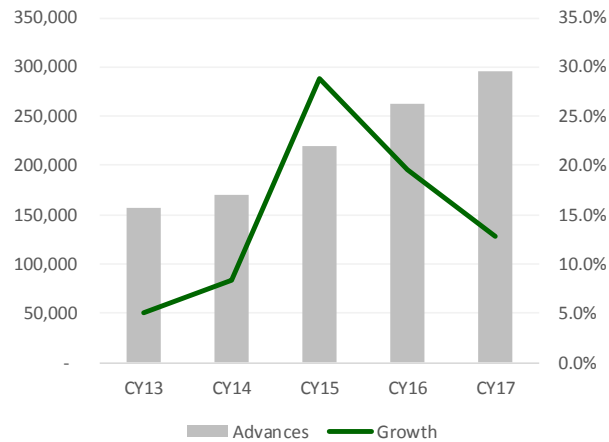
Going forward, keeping in view the slowdown in economy along with increase in interest rate we expect advances to grow at an average growth rate of 12 to 15 percent during CY19-CY21, with asset quality to improve further.

Fig.4 Categories of Advances by Group



Source: Co. Financials, Darson Research

Fig. 5 Advances vs Growth Rate YoY (Rs. In Mn)



Source: Co. Financials, Darson Research



Deposit Breakup	%
Government	54.9%
Individuals	26.3%
Construction	3.7%
Agribusiness	3.1%
PSEs	2.4%
Others	9.7%

Source: Co Financials, Darson Research

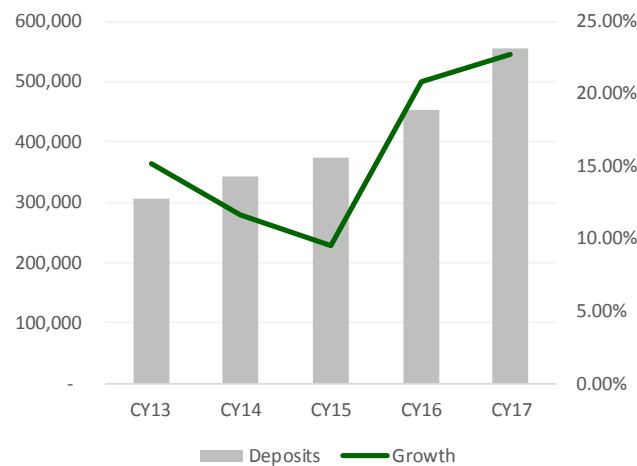
Impressive Deposits Growth with focus on Low Cost

BOP deposits have grown at a 5 year CAGR of 16% as compared to industry CAGR of 13% over the same period. Major contributors in deposits are PSEs and Federal and Provincial Govt. which contribute around 57% in total deposit base.

Saving deposits are the major contributor in total deposit with share of 43% in total deposit while fixed and current account contribute around 32% and 21% respectively. We forecast bank deposit to grow at an average rate of around 12 to 15 percent from CY19 to CY23 with the focus on current deposit as evident from the previous data that current account grew at the 5 year's average growth rate of 24% as compared to saving and fixed deposit growth rate of 19% and 7% respectively.

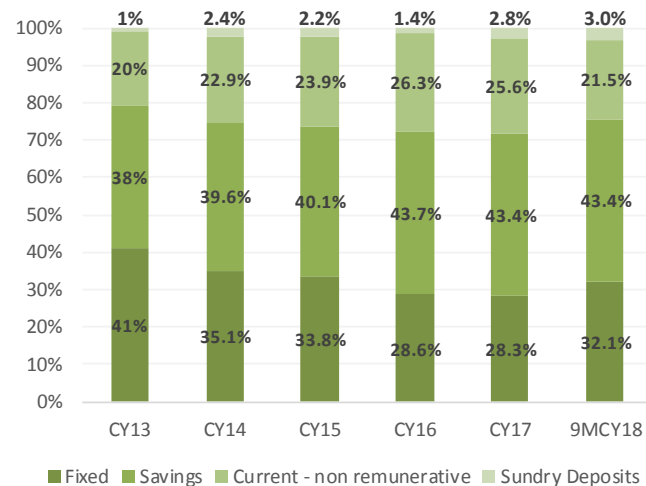
Bank's focus on low cost deposit resulted in improved CASA which moved to 71.73% in CY17 as compared to 58.23% in CY12. On other hand deposit cost declined from 7.45% in CY12 to 3.07% in CY17. We forecast CASA to further improve and may reach at 74% till CY23.

Fig. 6 Deposits and Deposit Growth YoY (Rs. in Mn)

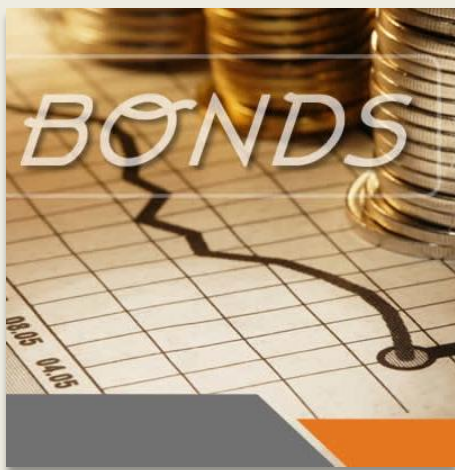


Source: Co. Financials, Darson Research

Fig. 7 Breakup of Deposit



Source: Co. Financials, Darson Research

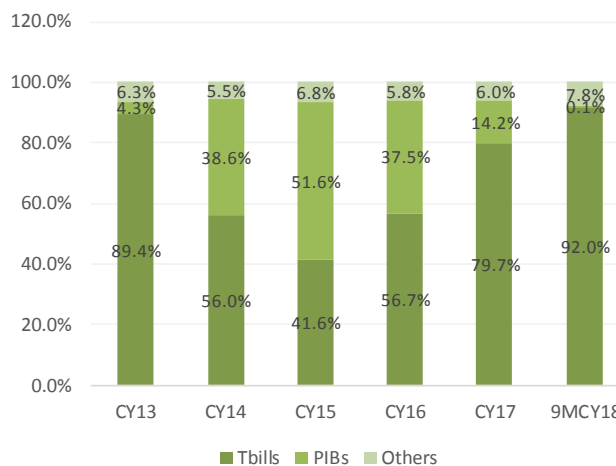


92% of Investments are in T-Bills

BOP currently holds 92% of its investment in T-Bills which is the highest in our banking universe (avg. of 57%). It places the bank in a well position to quickly reprice its investment base with the increase in yield on Govt. Papers.

BOP investment to deposit ratio (IDR) currently stands at around 35.63% we expect IDR may move to 40% till CY20, and expect bank shift its focus toward PIBs due to attractive yield. After a 425bps increase in policy rate we may expect another 50bps increase in 1QCY19 which will take the policy rate to 10.5%.

Fig. 8 Investment Breakup



Source: Co. Financials, Darson Research

Low cost to Income Ratio in Mid Tier Bank

Despite aggressive branch expansion the bank manages its cost. In CY17 bank's cost to income ratio was 50.23% which is below the average of Mid Tier Banks. Further during the years bank efficiently controlled its cost as its cost to income ratio down from 68% in CY13 to 50.23% in CY17. Going forward we expect bank cost to income ratio to remain around 50% during CY19 to CY23.

CAR Stand at 13.29% in Sep-18

After the loan scandal of 2008, BOP CAR ratio declined from 9.78% in CY07 to 1.92% in CY08 which was far below the SBP's required level of 9%. Keeping in view of the bank financial position and guarantee by GoPb, SBP gave relaxation to bank's on provision charge.

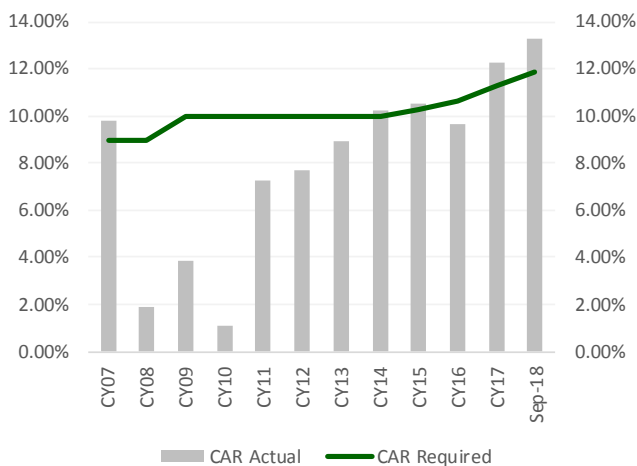
During last decade BOP met its CAR requirement only 2-3 times (see Fig. 9) and that was without total provision charge. In last 10years with the injection of Rs23bn equity and Rs8.8bn in the form of issuance of 10 years TFC and subordinated loan and improved profitability, bank first time met its CAR in CY17 after full provision charge.

We forecast BOP to continue to meet its CAR requirement but our expectation about payout in the form of cash dividend is not as probable.

Years	CAR Required	CAR Actual
CY07	9.00%	9.78%
CY08	9.00%	1.92%
CY09	10.00%	3.87%
CY10	10.00%	1.08%
CY11	10.00%	7.23%
CY12	10.00%	7.72%
CY13	10.00%	8.95%
CY14	10.00%	10.21%
CY15	10.25%	10.50%
CY16	10.65%	9.67%
CY17	11.28%	12.29%
Sep-18	11.90%	13.29%

Source: Co. Financials, Darson Research

Fig. 9 Actual vs Required CAR



Source: Co. Financials, Darson Research

Valuation

BOP is currently trading at CY18E/19E P/E and P/B of 4.83/3.8x and 0.94/0.75x. We have a BUY call on the stock with Dec-19 TP of Rs17.5%, providing potential upside of 33% from last day closing price.

We value BOP using Justified P/B methodology to arrive at our Dec-19 target price of Rs17.5/share. We arrived at Justified P/B multiple of around 0.99x by taking avg. ROE of around 19%, growth rate of 7.5% and cost of equity of 19.13%.

We have estimated cost of equity of 19.13% by using CAPM where we used 12% as risk free rate, 6% of risk premium and adjusted beta 1.19.

Assumptions	
Risk free Rate	12.0%
Market Risk Premium	6.00%
Adjusted Beta	1.19
Cost of Equity	19.1%
Average ROE	19.0%
Sustainable growth (g)	7.60%
Justified P/B	0.99
BVPS (Dec-19)	17.60
Target Price (Rs)	17.50

Source: Co Financials, Darson Research

Key Risks to our valuation

Higher than estimated provision on NPL

We incorporate provision in our earning estimate going forward, however any significant provision charge can decline our earning estimate and on the other hand any reversal in provision charge positively affect our earning estimate.

Lower than estimated deposit growth and change in deposit mix

We forecast deposit to grow at the average rate of around 12 to 15 percent in next 5 years by looking at the previous growth trend of bank. Any change in deposit mix, deterioration in macro economic indicator and slow down in M2 growth possibly affect the deposit growth and our valuation.

Change in regulatory requirements/implementation of IFRS 9

Introduction of IFRS 9 and any changes in regulatory requirement would affect our earning and valuation.

Financials Highlights

INCOME STATEMENT

(Rs in Mn)	CY14A	CY15A	CY16A	CY17A	CY18E	CY19F	CY20F
Markup/ Interest Earned	29,518	31,263	29,745	34,532	48,341	79,032	91,263
Markup/ Interest Expensed	(20,526)	(20,199)	(17,430)	(18,877)	(29,089)	(54,627)	(62,866)
Net Interest Income	8,992	11,064	12,315	15,655	19,253	24,404	28,397
Provisions	(1,178)	(3,529)	(1,020)	(14,223)	1,056	1,155	(205)
Non-Interest Income	2,800	7,635	5,301	4,604	3,977	4,625	5,045
Non-Interest Expenses	(6,253)	(7,671)	(8,529)	(10,731)	(12,579)	(15,185)	(17,256)
Loss/Profit Before tax	4,361	7,500	8,067	(4,696)	11,706	14,999	15,981
Taxation	(1,520)	(2,782)	(3,184)	1,379	(4,498)	(5,850)	(6,233)
Loss/Profit After Tax	2,842	4,718	4,883	(3,317)	7,208	9,149	9,749

BALANCE SHEET

	CY14A	CY15A	CY16A	CY17A	CY18E	CY19F	CY20F
Assets							
Cash & Balances	23,622	26,190	35,756	42,478	44,542	51,236	58,918
Investments	154,944	176,080	199,725	242,488	231,230	258,740	315,025
Advances (net)	170,273	219,356	262,190	295,841	393,284	457,004	506,609
Total Assets	420,400	472,283	545,447	649,709	714,047	824,030	949,488
Liabilities							
Borrowings from FIs	44,743	55,236	39,829	38,949	31,840	36,625	42,116
Deposits	342,291	374,961	453,174	556,192	612,642	704,711	810,380
Other Liabilities	10,282	15,521	15,792	16,864	19,902	22,893	26,326
Total Liabilities	401,044	449,606	517,479	619,870	677,079	777,509	892,776
Equity							
Share Capital	15,551	15,551	15,551	26,437	26,437	26,437	26,437
Reserves	2,081	2,329	1,117	3,297	3,297	3,297	3,297
Unappropriate profits	(9,083)	(5,221)	541	(3,035)	4,315	13,465	23,213
Surplus on reval. of assets	4,071	3,282	3,607	2,887	2,645	3,049	3,492
Total Liabilities & Equity	420,400	472,283	545,447	649,709	714,047	824,030	949,488

Source: Co. Financials, Darson Research

KEY RATIOS

	CY14A	CY15A	CY16A	CY17A	CY18E	CY19F	CY20F
EPS (Rs)	1.07	1.78	1.85	(1.25)	2.73	3.46	3.69
DPS (Rs)	-	-	-	-	-	-	-
BVPS (Rs)	7.32	8.58	10.58	11.29	13.98	17.60	21.45
P/E (x)	12.24	7.37	7.13	(10.49)	4.83	3.80	3.57
P/BV (x)	1.80	1.53	1.24	1.17	0.94	0.75	0.61
ROE (excluding surplus)	18.59%	24.32%	20.04%	-12.31%	21.00%	21.05%	18.32%
ROA	0.7%	1.0%	0.9%	-0.5%	1.0%	1.1%	1.0%
ADR	49.75%	58.50%	57.86%	53.19%	64.19%	64.85%	62.51%
IDR	45.27%	46.96%	44.07%	43.60%	37.74%	36.72%	38.87%
Yield on Earning Assets	7.73%	7.24%	5.80%	5.64%	7.07%	10.09%	10.16%
Cost of Funds	5.25%	4.65%	3.47%	3.13%	4.43%	7.24%	7.26%
Net Interest Margins (NIMs)	2.47%	2.59%	2.32%	2.51%	2.65%	2.85%	2.91%
Gross NPL Ratio	28.22%	22.78%	19.10%	15.30%	11.45%	9.63%	8.84%
NPL Coverage	48.02%	53.65%	56.41%	87.52%	88.86%	89.35%	89.35%

Source: Co. Financials, Darson Research

Important disclosures

This report has been prepared by Darson Securities (Pvt) Ltd. and is provided for information purposes only. Under no circumstances it is to be used or considered as an offer to sell, or a solicitation of any offer to buy. This information has been compiled from sources we believe to be reliable, but we do not hold ourselves responsible for its completeness or accuracy. All opinions and estimates expressed in this report constitute our present judgment only and are subject to change without notice. This report is intended for persons having professional experience in matters relating to investments.

Research Dissemination Policy:

Darson Securities (Pvt.) Ltd. endeavors to make all rightful efforts to disseminate research to all eligible clients in a timely manner through either electronic or physical distribution such as email, mail and/or fax. However, it is worth mentioning that, not all clients may receive the material at the same time.

Analyst Certification:

The research analyst(s), if any, denoted by AC on the cover of this report, who exclusively reports to the research department head, primarily involved in the preparation, writing and publication of this report, certifies that the expressed views in this report are unbiased and independent opinions of the analyst(s). The observations presented also accurately reflect the personal views of the analyst(s) based on the research about the subject companies/securities and in any case, no part of the compensation of the analyst(s) was, is, or will be directly or indirectly related to the inclusion of specific recommendations or views in this research report. It is also important to note that the research analyst(s) or any of its close relatives do not have a financial interest in the securities of the subject company aggregating more than 1% of the value of the company. Additionally, the research analyst or its close relative have neither served as a director/officer in the past 3 years nor received any compensation from the subject company in the past 12 months. The Research analyst or its close relatives have not traded in the subject security in the past 7 days and will not trade in next 5 days.

Financial Interest Disclosure:

Darson Securities (Pvt.) Ltd. or any of its officers and directors does not have a significant financial interest (above 1% of the value of the securities of the subject company). Darson Securities (Pvt.) Ltd., their respective directors, officers, representatives, employees and/or related persons may have a long or short position in any of the securities or other financial instruments mentioned or issuers described herein at any time and may make a purchase and/or sale, or offer to make a purchase and/or sale of any such securities or other financial instruments from time to time in the open market or otherwise.

Risk Associated with Target Price:

Any inability to compete successfully in their markets may harm the business. This could be a result of many factors which may include geographic mix and introduction of improved products or service offerings by competitors. The results of operations may be materially affected by global economic conditions generally, including conditions in financial markets. The company is exposed to market risks, such as changes in interest rates, foreign exchange rates and input prices.

Rating System:

- If;
- **Expected return >15%** - Buy Call
 - **Expected Return is in between 0% to 15%** - Neutral/Hold Call
 - **Expected Return <0%** - Sell Call

Valuation Methodology

To arrive at our period end target prices, DSL uses different valuation methodologies including:

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

SECP JamaPunji Portal link: www.JamaPunji.pk

Contact Details

MALIK DIL AWAYZ AHMED , CFA
Chief Executive Officer
Tel: +(92-21) 32471080-83
ceo@darsononline.com

YOUSUF SAEED
Research Analyst
Tel: +(92-21) 32467224
research@darsononline.com

SANTOSH KUMAR
Head of Institutional Sales
Tel: +(92-21) 32471086-87
santosh.kumar@darsononline.com

IMRAN KHAN
Head of Retail Sales
Tel: +(92-21) 32469678
imran.khan@darsononline.com