

**NATIONAL DEVELOPMENT BANK PLC [NDB.N0000]****MAINTAIN BUY****ACCELERATED CREDIT GROWTH PROPELS 3Q2021 EARNINGS...****Fair Value: 2022E - LKR 110.0 [+56%]**

Total Return with DPS: 2022E - 65% [AER 61%]

NDB's earnings saw an increase of 24%YoY in the 3Q2021 to LKR 1.8Bn while the surge was led by the growth in NII, Net Fee and Commission Income and Net Gain from Trading. However, impairment saw an increase of 52%YoY amidst the growth in lending portfolio and also in response to elevated risks caused by the pandemic. NDB recorded a strong loan growth of 14% for 9M2021 which was above our estimates. Consequently, we have upgraded our loan book growth target for 2021E up to 18%YoY and profits for 2021E were upgraded on the back of higher earnings in 3Q2021 above our estimates. Nevertheless, taking into account the higher risk-free rate applicable for valuations with the rise in interest rates, we have downgraded NDB's fair value for 2022E to LKR 110.0 (from previous LKR 127.0) **MAINTAIN BUY**

LKR (Mn)	3Q2020	3Q2021	YoY	9M2020	9M2021	YoY
<b>Earnings (LKR 'Mn)</b>						
Net Interest Income	4,890	5,610	+15%	13,811	16,017	+16%
Total Operating Income	7,164	8,386	+17%	19,923	24,586	+23%
Post Impairment Income	5,515	5,885	+7%	15,109	17,940	+19%
Pre Tax Profit	2,377	2,525	+6%	5,921	7,766	+31%
Net Profit	1,505	1,872	+24%	3,869	5,968	+54%
<b>Balance Sheet (LKR 'Mn)</b>						
Loans	425,870	486,575	+14%	425,870	486,575	+14%
Shareholders' Equity	46,726	61,886	+32%	46,726	61,886	+32%
NAVPS	130.8	173.3	+32%	131	173.3	+32%

**Earnings surged by 24%YoY led by the growth in Total Operating Income**

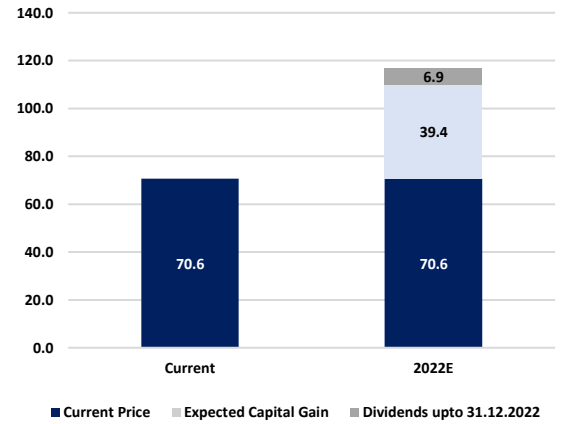
NDB recorded a surge in earnings by 24%YoY owing to the improvement in NII (15%YoY) to LKR 5.6Bn while, NII benefitted by a larger reduction in interest expenses by 12%YoY to LKR 7.7Bn driven by the timely re-pricing of assets and liabilities, together with NDB's continually strengthening CASA base (38%YoY growth). Net Fee and Commission Income growth (17%YoY) to LKR 1.8Bn was led by the enhanced business volumes reflected in gross loans growth of 14%YTD. Trade finance activities were the main contributor towards enhanced fees, whilst accelerated digital banking usage by customers also supported the fee drive. Net gains and trading also posted an increase of 273%YoY over 3Q2020 to LKR 902.0Mn, reflecting the forex income gained during the quarter. However, impairment charges recorded an increase of 52%YoY to LKR 2.5Bn in line with the growth in the loan provisions provided at both collective and individual levels in response to elevated risks caused by the pandemic and other stresses.

**Loan growth was upgraded to 18% for 2021E and 15% for 2022E**

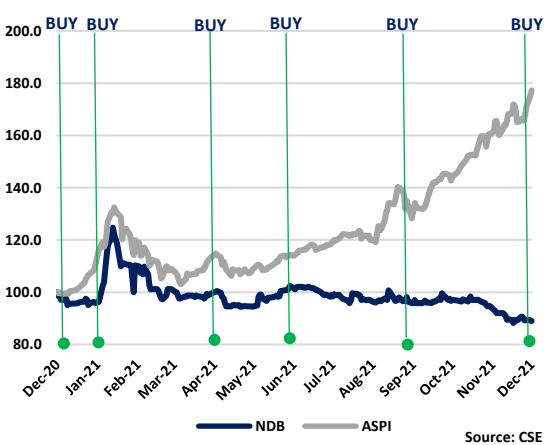
Capital infusion of LKR 9.5Bn from the rights issue and private placement in 2Q2021 lifted NDB's Tier 1 ratio to 10.03% by 3Q2021 from 9.73% recorded at end-2020 and is expected to act as a cushion driving the future loan book growth. With its aggressive plans of increasing the market share, we expect NDB to clock a loan growth of 18% in 2021E and 15% in 2022E above the private sector credit growth expectation of c.12%. Hence, we expect NII to improve amidst the strong loan book growth and potential rise in interest rates and thereby NII for 2021E and 2022E are expected to record a growth of 24%YoY and 14%YoY respectively.

**Fair Value for 2022E was downgraded to LKR 110.0– MAINTAIN BUY**

We have adjusted for the proposed surcharge tax of 25% (LKR 1.8Bn) in retained earnings of 2021E and VAT increase through 2022E earnings. We haven't adjusted for the 2.5% Social Security Contribution (SSC) considering the fact that it is not finalised yet and it will be passed on to the customer through increased interest rates and other applicable fees and commission. Hence 2022E earnings were revised down to LKR 8.8Bn from previous estimates, amidst the VAT increase of 15% to 18% impacting the bottom line. Moreover, considering the potential higher interest rates impacting higher risk-free rate applicable for valuations, we have downgraded NDB's fair value to LKR 110.0 for 2022E. However, at the current market price of LKR 70.6, 2022E fair values imply an upside of 56% and trades well below its current book value of LKR 173.3 with a PBV of 0.4x. **MAINTAIN BUY**

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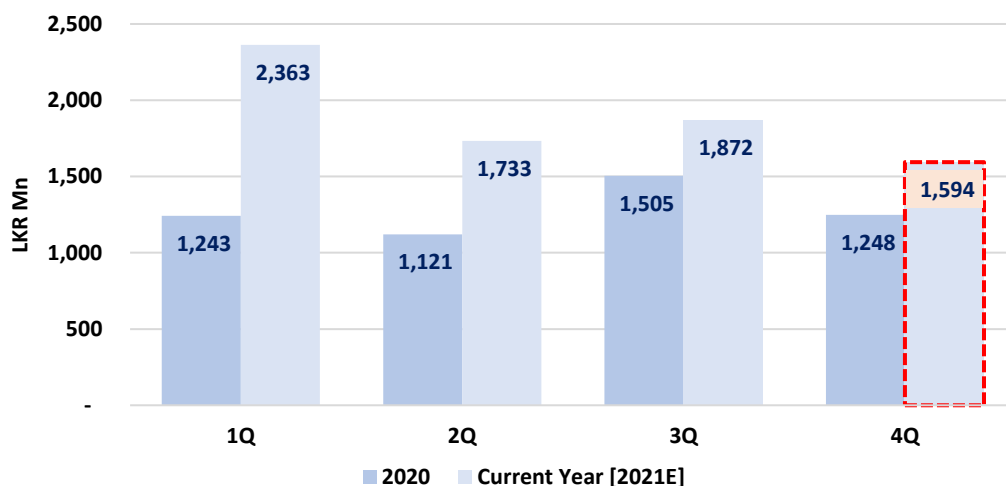
[hiruni@firstcapital.lk](mailto:hiruni@firstcapital.lk)**Price performance of NDB vs ASPI and past recommendations****Minimum Return for BUY:**

**Buy Below for 2022E [AER of 14.8% with DPS]: LKR 101.0**  
NDB categorized as 'Grade A' counter

**Disclosure on Shareholding:**

First Capital Group or the covering analyst did not hold 1% or more of the total outstanding share capital of NDB during the five trading days prior to the issuance of this document.

## Quarterly Earnings



## Estimate Revision

In LKR Mn	2021E - O	2021E - R	% Change	2022E - O	2022E - R	% Change
<b>Earnings Estimate</b>						
Net Interest Income	21,266	22,174	+4%	24,780	25,251	+2%
Total Operating Income	30,465	33,542	+10%	34,579	37,892	+10%
Post Impairment Income	23,483	24,153	+3%	27,980	28,635	+2%
Pre Tax Profit	9,973	10,146	+2%	12,805	11,914	-7%
Net Profit	6,900	7,562	+10%	8,859	8,880	+0%
Adjusted EPS	19.3	21.2		24.8	24.9	
Net Profit Growth YoY	35%	48%		28%	17%	
<b>Balance Sheet Estimate</b>						
Loans & Advances	489,678	496,144	1%	549,976	565,406	+3%
Shareholders' Equity	64,369	62,625	-3%	70,986	69,046	-3%
<b>NAVPS (adjusted)</b>	<b>180.2</b>	<b>175.4</b>		<b>198.8</b>	<b>193.3</b>	
<b>Ratio Estimate</b>						
<b>ROE (%)</b>	<b>12.2%</b>	<b>13.7%</b>		<b>13.1%</b>	<b>13.5%</b>	
<b>PER (x)</b>	<b>4.0</b>	<b>3.3</b>		<b>3.1</b>	<b>2.8</b>	
<b>PBV (x)</b>	<b>0.4</b>	<b>0.4</b>		<b>0.4</b>	<b>0.4</b>	

## Valuation Table

P/E 31 December	2017	2018	2019	2020	2021E	2022E	2023E
<b>Estimates (LKR 'Mn)</b>							
Net Interest Income	11,086	15,104	17,971	17,925	22,174	25,251	28,249
Total Operating Income	16,683	22,553	24,806	26,404	33,542	37,892	42,510
<b>Net Profit</b>	<b>3,490</b>	<b>5,136</b>	<b>4,776</b>	<b>5,117</b>	<b>7,562</b>	<b>8,880</b>	<b>12,022</b>
Adjusted EPS (LKR)	9.8	14.4	13.4	14.3	21.2	24.9	33.7
Net Profit YoY Growth (%)	30%	47%	-7%	7%	48%	17%	35%
<b>Valuations</b>							
PER (x)	7.2x	4.9x	5.3x	4.9x	3.3x	2.8x	2.1x
PBV (x)	0.8x	0.6x	0.6x	0.5x	0.4x	0.4x	0.3x
DY (%)	12.7%	11.3%	9.9%	2.1%	9.8%	11.4%	15.5%
NAVPS	92.4	109.5	121.5	134.3	175.4	193.3	218.9
Adjusted DPS	4.3	4.7	4.3	1.0	6.9	8.1	10.9
Dividend Payout	44%	33%	33%	7%	33%	33%	33%

## Valuation Summary

Expected NDB price	2022E
Justified PBV based target price	100.4
PER Valuation based target price	111.9
RI Valuation based target price	115.1
<b>Average Target Price</b>	<b>109.1</b>
<b>Target Price after Rounding off</b>	<b>110.0</b>

Return	2022E
Target Price	110.0
Current Price	70.6
Capital Gain (LKR)	39.4
Dividends upto 31st Dec (LKR)	6.9
Capital Gain %	56%
Dividend Yield %	10%
<b>Total Return %</b>	<b>65%</b>
Annualized Return %	61%

## Residual Income Valuation

Residual Income based Valuation	2022E
PV of Residual Income	-21,525
No. of Shares ('Mn)	357
RI per Share	-60.3
Opening Book value per Share	175.4
<b>Value per Share</b>	<b>115.1</b>

COE	2022E
Rf	10.0%
Rm	18.0%
Growth %	3.0%
$\beta$	1.65
$Ke=Rf+\beta(Rm-Rf)$	23.2%

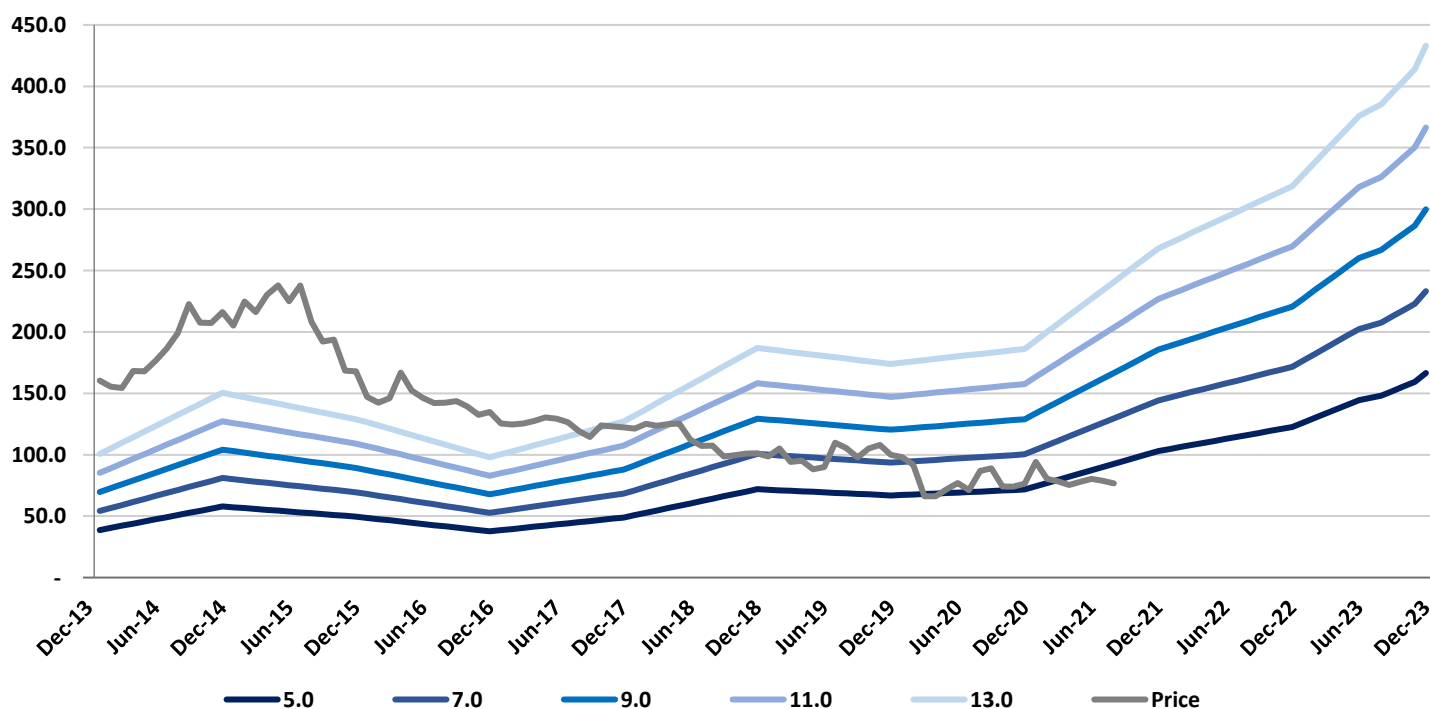
## Justified PBV Valuation

Justified PBV based Valuation	2022E
ROAE	13.5%
Growth	3.0%
COE	23.2%
PBV	0.52
NAVPS	193.3
<b>Target Price</b>	<b>100.4</b>

## PER Valuation

PER based Valuation	2022E
Earnings (LKR 'Mn)	8,880
No. of Shares ('Mn)	357
EPS	24.9
Expected PER	4.5x
<b>Price at 4.5x of Earnings</b>	<b>111.9</b>

## PER Chart



## Appendix I: Statement of Income and Expenses

Statement of Financial Performance (LKR Mn)	2017	2018	2019	2020	2021E	2022E	2023E
<b>P/E 31st Dec</b>							
<b>Gross Income</b>	<b>42,445</b>	<b>51,621</b>	<b>60,237</b>	<b>61,632</b>	<b>65,302</b>	<b>77,401</b>	<b>89,146</b>
Interest Income	37,421	44,622	53,402	53,153	53,934	64,760	74,886
Interest Expenses	-26,335	-29,518	-35,431	-35,228	-31,760	-39,509	-46,637
<b>Net Interest Income</b>	<b>11,086</b>	<b>15,104</b>	<b>17,971</b>	<b>17,925</b>	<b>22,174</b>	<b>25,251</b>	<b>28,249</b>
Fee & Other Income	5,597	7,450	6,836	8,479	11,368	12,641	14,261
<b>Total Operating Income</b>	<b>16,683</b>	<b>22,553</b>	<b>24,806</b>	<b>26,404</b>	<b>33,542</b>	<b>37,892</b>	<b>42,510</b>
Impairment (Charges)/ Reversal	-1,290	-3,765	-4,405	-6,794	-9,388	-9,257	-8,301
<b>Net Operating Income</b>	<b>15,393</b>	<b>18,788</b>	<b>20,401</b>	<b>19,610</b>	<b>24,153</b>	<b>28,635</b>	<b>34,209</b>
Less : Operating expenses							
Personal Expenses	-4,025	-4,898	-5,460	-5,748	-6,481	-7,518	-8,386
Depreciation and Amortization	-478	-509	-883	-932	-908	-984	-1,069
Other Operating Expenses	-3,698	-3,959	-4,065	-3,721	-4,317	-4,747	-5,219
<b>Op. profit before value added tax</b>	<b>7,192</b>	<b>9,422</b>	<b>9,992</b>	<b>9,209</b>	<b>12,448</b>	<b>15,386</b>	<b>19,535</b>
VAT on financial services	-1,547	-1,938	-2,068	-1,819	-2,302	-3,472	-3,406
Debt Repayment Levy	0	-235	-1,003	0	0	0	0
<b>Op. profit after value added tax</b>	<b>5,644</b>	<b>7,248</b>	<b>6,921</b>	<b>7,390</b>	<b>10,146</b>	<b>11,914</b>	<b>16,129</b>
Share of associate companies' profit	0	0	0	0	0	0	0
<b>Profit Before Tax</b>	<b>5,644</b>	<b>7,248</b>	<b>6,921</b>	<b>7,390</b>	<b>10,146</b>	<b>11,914</b>	<b>16,129</b>
Income Tax Expense	-2,212	-1,972	-2,036	-2,173	-2,435	-2,859	-3,871
<b>Profit for the Year</b>	<b>3,432</b>	<b>5,276</b>	<b>4,885</b>	<b>5,217</b>	<b>7,711</b>	<b>9,054</b>	<b>12,258</b>
Minority Interest	-57	140	109	101	149	174	236
<b>Profit attributable to Equity Holders</b>	<b>3,490</b>	<b>5,136</b>	<b>4,776</b>	<b>5,117</b>	<b>7,562</b>	<b>8,880</b>	<b>12,022</b>
<b>Adjusted EPS</b>	<b>9.8</b>	<b>14.4</b>	<b>13.4</b>	<b>14.3</b>	<b>21.2</b>	<b>24.9</b>	<b>33.7</b>

## Appendix II: Statement of Financial Position

Balance Sheet (LKR Mn)	2017	2018	2019	2020	2021E	2022E	2023E
<b>As at 31st December</b>							
<b>ASSETS</b>							
Cash and cash equivalents	5,343	7,170	6,081	10,779	9,966	16,462	16,592
Balances with Central Bank	15,365	15,546	13,887	6,812	21,251	24,291	26,693
Placements with banks	841	15,237	6,291	12,402	11,458	10,266	5,544
Derivative financial instruments	2,472	3,938	1,596	1,429	1,672	1,873	2,023
Financial assets recognised through profit or loss	2,660	4,052	3,489	7,713	9,024	10,107	10,916
Loans and advances to customers	274,079	344,276	396,672	425,682	496,144	565,406	617,304
Financial assets at amortised costs	23,316	24,175	27,486	44,712	52,313	38,499	38,114
Financial assets measured at Fair value through OCI	52,976	54,487	68,430	108,763	127,253	142,523	153,925
Other assets	2,275	2,933	3,228	3,595	4,206	4,711	5,088
Intangible assets	397	397	701	1,062	1,038	1,007	969
Deferred tax	0	1,101	647	1,946	1,946	1,946	1,946
Property, plant & equipment	2,917	3,144	3,565	3,541	3,336	3,149	2,955
Investment properties	1,895	2,111	2,273	2,362	2,362	2,362	2,362
<b>Total assets</b>	<b>388,645</b>	<b>478,596</b>	<b>535,600</b>	<b>632,132</b>	<b>742,828</b>	<b>823,462</b>	<b>885,287</b>
<b>LIABILITIES</b>							
Due to Banks	20,237	15,047	18,380	24,173	26,174	30,141	33,581
Derivative financial instruments	937	2,907	729	1,017	1,185	1,351	1,474
Due to customers	273,041	347,170	404,668	489,659	572,901	641,649	692,981
Debt securities issued and other borrowed funds	28,107	43,423	30,740	35,784	38,963	38,247	37,209
Tax liabilities	1,575	3,175	2,342	2,563	2,872	3,373	4,566
Other liabilities	9,177	8,838	9,807	8,435	9,831	11,203	12,232
Subordinated term debts	19,337	16,812	23,109	19,881	25,485	25,485	21,859
Deferred Tax	1,796	513	567	596	596	596	596
Employee benefit liabilities	460	502	719	820	820	820	820
<b>Total liabilities</b>	<b>354,667</b>	<b>438,386</b>	<b>491,061</b>	<b>582,928</b>	<b>678,828</b>	<b>752,865</b>	<b>805,319</b>
<b>EQUITY ATTRIBUTABLE TO PARENT</b>							
Stated capital	2,209	6,469	7,685	8,794	18,264	18,264	18,264
Statutory reserve fund	1,336	1,636	1,896	2,196	2,196	2,196	2,196
Investment Fund	886	337	571	842	842	842	842
Retained Earnings	28,581	30,668	33,230	36,143	41,322	47,744	56,879
<b>Equity attributable to parent</b>	<b>33,012</b>	<b>39,111</b>	<b>43,383</b>	<b>47,976</b>	<b>62,625</b>	<b>69,046</b>	<b>78,181</b>
Non-controlling interests	966	1,099	1,155	1,227	1,376	1,550	1,786
<b>Total Equity</b>	<b>33,978</b>	<b>40,210</b>	<b>44,539</b>	<b>49,203</b>	<b>64,000</b>	<b>70,596</b>	<b>79,968</b>
<b>Total liabilities and total equity</b>	<b>388,645</b>	<b>478,596</b>	<b>535,600</b>	<b>632,132</b>	<b>742,828</b>	<b>823,462</b>	<b>885,287</b>
<b>Adjusted NAVPS</b>	<b>92.4</b>	<b>109.5</b>	<b>121.5</b>	<b>134.3</b>	<b>175.4</b>	<b>193.3</b>	<b>218.9</b>



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