



First Capital
A Janashakthi Group Company

COMMERCIAL BANK OF CEYLON PLC [COMB.N0000]

MAINTAIN BUY

“LEADER IN LENDING”

Fair Value: 2024E - LKR 165.0 [+56%]

2025E - LKR 190.0 [+79%]

Total Return with DPS: 2024E - 65% [AER 143%]

2025E - 91% [AER 51%]

COMB Rights Issue: In an announcement to CSE, Commercial Bank of Ceylon announced a Right Issue of 1 for every 5 shares held for both the voting and non-voting shares. The company expects to raise LKR 22.5Bn from the rights issue, which will be utilized to increase the Tier 1 Capital and the total capital of the company in order to accommodate and facilitate future business growth.

With the assumption that all proceeds from RI is invested towards COMB capital, we believe that there is a possibility that current tier 1 capital ratio will rise to 12.95% from 1Q2024 ended 11.46% (regulatory requirement 10.00%).

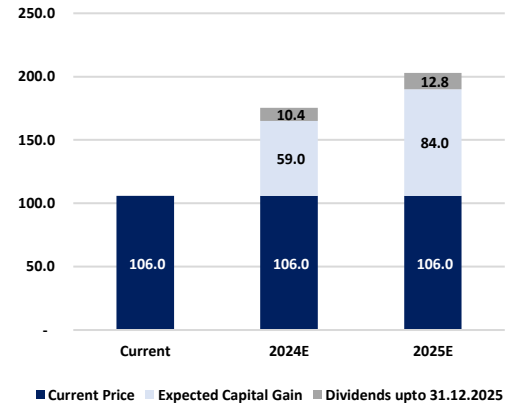
Moreover, the proposed Rights issue is expected to downward adjust the book value of COMB to LKR 155.4 for 2024E (from LKR 165.1) and LKR 165.4 for 2025E (from 173.4). Thus, in line with the downward adjustment of the net asset value, we are revising down our Rights adjusted target price for 2024E to LKR 165.0 (from LKR 170.0) and 2025E to LKR 190.0 (from LKR 200.0).

COMB net earnings recorded a significant growth of 152.0%YoY to LKR 10.6Bn beating our estimate of LKR 5.5Bn set for 1Q2024. In line with our expectations, reduction in impairments (-49.5%YoY to LKR 3.4Bn) continued to remain a key catalyst for profitability whilst higher than expected NIMs, enabled COMB to outperform our estimates. Going forward, we expect reduction in impairments to drive the profitability of COMB higher whilst, the expected pick up in loan book during 2H2024, is expected to support core business growth. Meanwhile, considering the attractive valuations on the share (trading at a 35.8% discount to 2025E book value of LKR 165.3), and positive outlook for the bank, we continue to remain bullish on COMB and arrived at a RI adjusted TP of LKR 165.0 for 2024E and LKR 190.0 for 2025E. Thus, we continue to rate COMB MAINTAIN BUY.

LKR (Mn)	1Q2023	1Q2024	YoY	2022	2023	YoY
Earnings (LKR 'Mn)						
NII	18,975	27,698	+46%	84,665	86,415	+2%
Total Operating Income	25,287	34,947	+38%	136,637	122,070	-11%
Net Operating Income	18,490	31,511	+70%	64,712	83,175	+29%
PBT	6,741	16,738	+148%	24,505	33,927	+38%
Net Profit	4,216	10,627	+152%	23,812	21,115	-11%
Balance Sheet (LKR 'Mn)						
Shareholder's Equity	205,148	220,833	+8%	208,865	220,471	+6%
NAVPS	123.0	132.4	+8%	123.0	132.4	+8%

COMB earnings jump by 152.0%YoY during 1Q2024

COMB net earnings for 1Q2024 recorded a significant growth of 152.0%YoY to LKR 10.6Bn, beating our estimate of LKR 5.5Bn for the quarter. The outperformance of COMB earnings for 1Q2024 was largely due to faster than anticipated growth in Net Interest Income, which recorded a growth of 46.0%YoY to LKR 27.7Bn. Timely repricing of deposit products and lag effect in pricing lending products enabled COMB to expand NIMs (improved to 4.22% from 3.32% in 4Q2023 and 3.05% in 1Q2023), which boosted the NII for COMB during 1Q2024. Moreover, impairment charges for 1Q2024 recorded a steep decline of 49.5%YoY to LKR 3.4Bn, largely due to the higher base effect in 1Q2023, as a result of higher provisions made for foreign currency bonds. Furthermore, a steady improvement in Net Fee and Commission was also observed on COMB 1Q2024 results (4.3%YoY), despite the appreciation in LKR (LKR has appreciated by 7.3%YTD against the dollar) witnessed during the Jan-May 2024 period. Meanwhile, escalation in operating expenses (+12.9%YoY) and increase in taxes (VAT on financial services up by 153.6%YoY whilst corporate taxes increased by 148.9%YoY) were amongst the causes, which negatively impacted COMB profitability during 1Q2024.



FIRST CAPITAL RESEARCH

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Price Movement of COMB vs ASPI (Indexed and Rebased to 100)



Source: CSE

Minimum Return for BUY:

Buy Below 2024E - [AER of 19% with DPS]: LKR 154.0
COMB.N 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 COMB during the five trading days prior to the issuance of this document.



Gross loan book accelerates during 1Q2024

The gross loan book of COMB accelerated for the 2nd consecutive session and grew by 10.9%YoY (+1.6%QoQ) to LKR 1.3Tn. The growth in loan book was largely driven by the acceleration of domestic lending book, which recorded an uptick of 15.7%YoY (+3.9%QoQ) in 1Q2024 to LKR 943.9Bn. The growth in loan book was triggered mainly by the reduction in interest rates (AWLR declined to 13.43% in 1Q2024 end from 14.21% in 4Q2023) and the expansion of GDP activity in the country. However, with the improvement in the external position of Sri Lanka, LKR appreciated by 7.3% cf. the USD, which adversely affected foreign currency denominated lending products and resulted in a marginal growth of 0.2%YoY (-4.0%QoQ) to LKR 372.3Bn. Meanwhile, in line with our expectations, NPL ratio of COMB continued to edge down and recorded at 5.59% in 1Q2024 cf. 5.85% recorded in 4Q2023.

COMB deposit base expanded by 5.8%YoY to LKR 2.1Tn

COMB deposit base expanded by 5.8%YoY to LKR 2.1Tn in 1Q2024 driven predominantly by local currency denominated deposits, which grew by 11.0%YoY and 2.9%QoQ to LKR 1.4Tn. The growth in deposits during the period was driven by expansion in deposit products across all segments. However, as a result of LKR appreciation, foreign currency denominated deposits contracted by 3.6%YoY and 6.5%QoQ during 1Q2024. Meanwhile, backed by the growth in LC denominated current and savings account base, CASA ratio of COMB improved to 40.94% in 1Q2024 from 39.74% recorded in 4Q2023 and 37.81% in 1Q2023. The improvement in NIMs during the period was also driven by the expansion in CASA ratio.

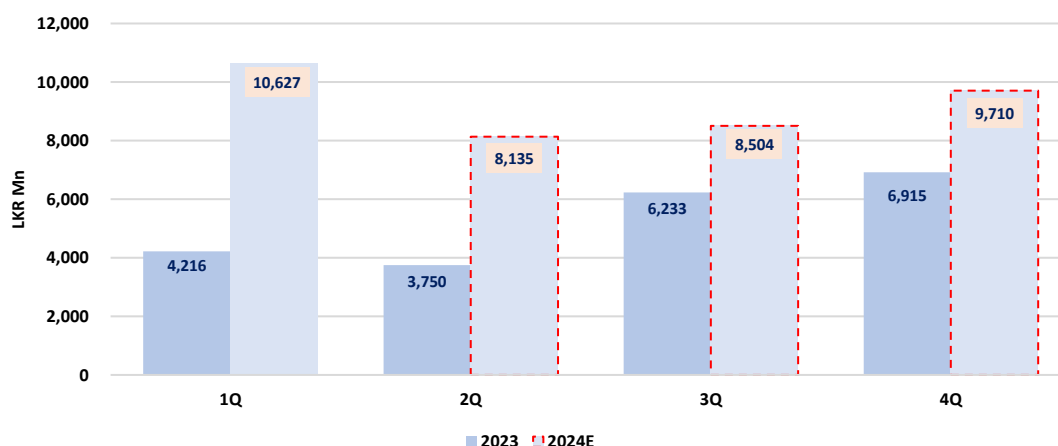
Announced rights Issue to strengthen the capital buffers

As mentioned above, with the announced RI, COMB Tier 1 capital ratio is expected to strengthen to 12.95% from 1Q2024 ended 11.46% (regulatory requirement 10.00%). COMB's Total Capital Ratio is also expected to improve, strengthening to 16.35% from 14.86% recorded at 1Q2024 end (regulatory requirement 14.00%).

Earnings revised up; TP revised down due to announced RI

Having beaten our 1Q2024 estimates, largely due to higher spreads, we revised up our estimates for 2024E to LKR 37.0Bn (up from LKR 27.5Bn) and 2025E to LKR 43.3Bn (from previous LKR 33.6Bn). With continuous pressure from CBSL to reduce lending rates (given that AWPLR has fallen below 10%), we believe there can be a contraction in spreads in the coming months, which can result in a contraction of NIMs. We believe this will moderate NII growth in the coming months, yet an expansion in loan book amidst a recovery in economy is expected to offset the fall in NIMs. Moreover, we believe, reduction in new impairments will continue to remain a key catalyst for the COMB performance in the coming months. Considering the positive outlook for the bank we continue to be bullish on COMB. Therefore, considering the new shares issued via rights, we have arrived at a RI adjusted TP of LKR 165.0 for 2024E, adjusted down from LKR 170.0 and 2025E TP to LKR 190.0 from LKR 200.0. Considering the substantial discount to our TP we continue to **maintain our recommendation at BUY.**

Quarterly Earnings



Estimate Revision

In LKR Mn	2024E-O	2024E-R	% Change	2025E-O	2025E-R	% Change
Earnings Estimate						
NII	86,426	106,404	+23%	105,468	125,351	+19%
Total Operating Income	121,111	143,186	+18%	143,554	165,525	+15%
Net Operating Income	105,097	122,313	+16%	122,744	141,385	+15%
Profit before Tax	47,666	64,194	+35%	58,286	75,994	+30%
Net Profit	27,456	36,976	+35%	33,573	43,773	+30%
Adjusted EPS	20.9	28.1		25.5	33.3	
Balance Sheet Estimate						
Shareholders' Equity	231,064	259,138	+12%	258,452	293,773	+14%
Adjusted NAVPS	165.1	155.4		173.4	165.4	

Valuation Table

P/E 31st December	2020	2021	2022	2023	2024E	2025E	2026E
Estimates (LKR 'Mn)							
Net Interest Income	48,640	66,416	84,665	86,415	106,404	125,351	146,909
Total Operating Income	74,500	93,598	136,637	122,070	143,186	165,525	190,965
Net Profit: Equity Holders	16,940	24,062	23,812	21,115	36,976	43,773	52,536
Adjusted EPS (LKR)	12.9	18.3	18.1	16.1	28.1	33.3	40.0
YoY Growth (%)	-2%	42%	-1%	-11%	75%	18%	20%
Valuations							
PER (x)	8.2x	5.8x	5.8x	6.6x	3.8x	3.2x	2.7x
PBV (x)	1.1x	1.1x	0.8x	0.8x	0.7x	0.6x	0.6x
DY (%)	6.1%	7.1%	4.2%	6.1%	9.8%	12.1%	14.2%
Adjusted NAVPS (LKR)	95.2	100.4	125.3	132.2	155.4	165.4	176.2
DPS (LKR)	6.5	7.5	4.5	6.5	10.4	12.8	15.0
Dividend Payout (%)	50.4%	41.0%	24.8%	40.5%	36.9%	38.5%	37.6%

Valuation Summary

Expected COMB.N Price	2024E	2025E
Justified PBV based target price	155.4	182.0
PER Valuation based target price	177.4	197.2
RI Valuation based target price	166.6	198.7
Average Target Price	166.5	192.6
Target Price after Rounding off	165.0	190.0

Return	2024E	2025E
Target Price	165.0	190.0
Current Price	106.0	106.0
Capital Gain (LKR)	59.0	84.0
Dividends upto 31st Dec (LKR)	10.4	12.8
Capital Gain %	56%	79%
Dividend Yield %	10%	12%
Total Return %	65%	91%
Annualized Return %	143%	51%

Residual Income Valuation

Residual Income based Valuation	2024E	2025E
PV of Residual Income	57,309	76,806
No. of Shares ('Mn)	1,667	1,776
RI per Share	34.4	43.3
Opening Book Value per Share	132.2	155.4
Value per Share	166.6	198.7

COE	2024E	2025E
Rf	11.0%	11.0%
Rm	19.0%	19.0%
Growth %	3.0%	3.0%
β	0.8	0.8
$Ke=Rf+\beta(Rm-Rf)$	17.4%	17.4%

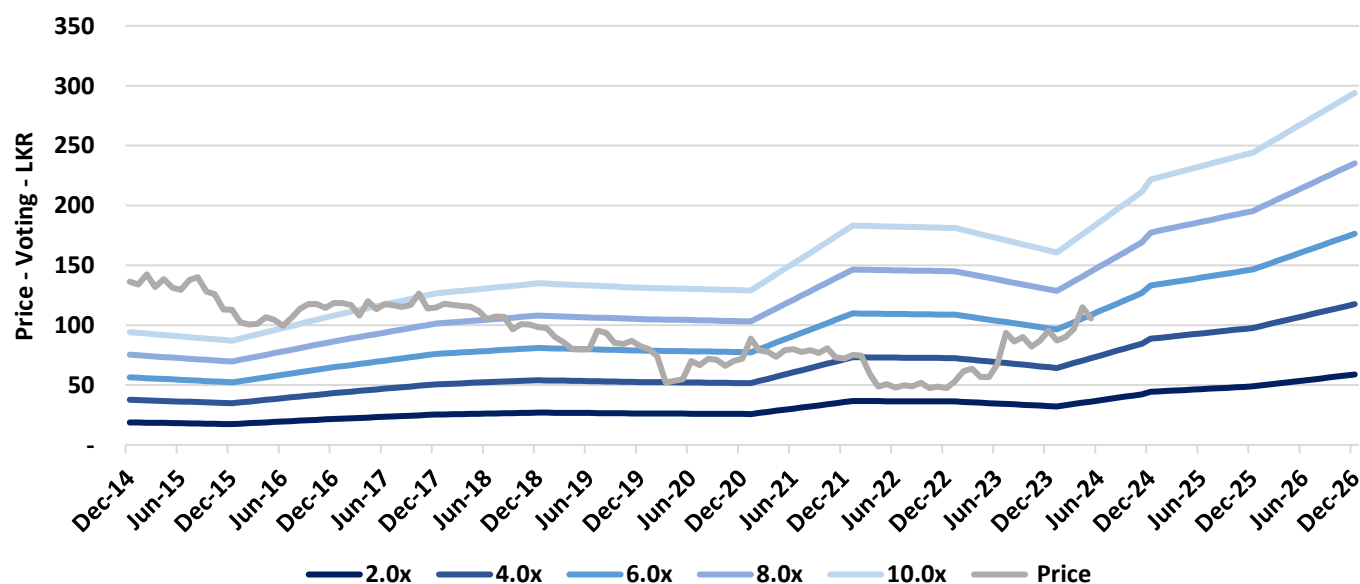
Justified PBV Valuation

Justified PBV based Valuation	2024E	2025E
ROAE	15.4%	15.8%
Growth	3.0%	3.0%
COE	17.4%	17.4%
PBV	1.0	1.1
NAVPS	155.4	165.4
Target Price	155.4	182.0

PER Valuation

PER based Valuation	2024E	2025E
Earnings (LKR 'Mn)	36,976	43,773
No. of Shares ('Mn)	1,667	1,776
EPS	22.2	24.6
Expected PER	8.0x	8.0x
Price at 8.0x Earnings	177.4	197.2

PER Chart



Appendix I: Statement of Income and Expenses

Income Statement P/E 31st December	2020	2021	2022	2023	2024E	2025E	2026E
Gross Income	149,737	163,675	280,387	341,566	312,466	355,173	410,951
Interest Income	121,858	132,818	222,393	297,646	266,672	305,536	356,960
Less: Interest Expenses	73,219	66,402	137,728	211,231	160,268	180,185	210,051
Net Interest Income	48,640	66,416	84,665	86,415	106,404	125,351	146,909
Net Fee and Commission Income	9,822	12,242	20,169	22,387	23,174	24,333	25,549
Total Operating Income	74,500	93,598	136,637	122,070	143,186	165,525	190,965
Less: Impairment Charge/(Reversal) for Loans	21,420	25,140	71,924	38,895	20,873	24,140	25,821
Net Operating Income	53,081	68,458	64,712	83,175	122,313	141,385	165,144
Less : Operating Expense							
Personnel Expenses	14,993	16,799	19,788	22,825	29,207	31,620	34,137
Other Operating Expenses	11,270	12,859	16,494	21,465	25,024	28,111	31,803
Total Operating Expenses	26,263	29,658	36,282	44,290	54,232	59,731	65,940
Operating Profit before Value Added Tax (VAT)	26,818	38,801	28,430	38,885	68,082	81,654	99,204
Less: Value Added tax on Financial Services	4,531	5,845	3,921	4,961	3,892	5,664	8,000
Operating Profit after Value Added Tax (VAT)	22,287	32,955	24,509	33,924	64,190	75,990	91,204
Profit before Income Tax	22,291	32,957	24,505	33,927	64,194	75,994	91,208
Less: Income Tax Expense	7,433	8,667	106	12,027	25,678	30,398	36,483
Profit for the Year	14,858	24,290	24,399	21,900	38,516	45,597	54,725
Non-Controlling Interest	(2,082)	228	588	785	1,541	1,824	2,189
Profit Attributable to Equity Holders	16,940	24,062	23,812	21,115	36,976	43,773	52,536
Adjusted EPS	12.9	18.3	18.1	16.1	28.1	33.3	40.0

Appendix II: Statement of Financial Position

Statement of Financial Position P/E 31st December	2020	2021	2022	2023	2024E	2025E	2026E
ASSETS							
Cash and Cash Equivalents	50,817	69,335	151,109	159,702	173,101	89,622	57,985
Balances with Central Banks	115,359	56,777	78,597	62,634	77,011	95,509	107,881
Placements with Banks	16,422	12,499	96,083	81,507	73,356	66,020	59,418
Derivative Financial Instruments	2,637	3,245	8,345	7,226	6,089	6,698	7,703
Other Financial Assets Held-For-Trading	35,189	23,436	24,873	29,450	33,830	37,212	42,794
Loans and Receivables to Other Customers	909,829	1,029,584	1,155,493	1,204,866	1,378,355	1,562,832	1,740,859
Financial Investments - Available-for-sale	278,717	335,954	118,652	287,733	631,485	694,633	798,828
Property, Plant & Equipment	25,387	24,745	27,447	28,997	28,813	28,406	27,777
Intangible Assets	1,801	2,273	4,113	4,289	4,026	3,729	3,394
Other Assets	20,195	27,083	40,811	37,736	45,106	37,212	42,794
Total assets	1,762,058	1,983,491	2,499,554	2,655,612	2,861,036	3,169,754	3,630,159
LIABILITIES							
Securities Sold Under Repurchase Agreements	91,412	151,425	97,726	111,187	110,268	125,027	139,269
Due to Other Customers	1,286,616	1,472,640	1,977,744	2,147,907	2,255,302	2,480,832	2,852,957
Subordinated Term Debts	38,247	38,303	61,401	36,483	41,351	46,885	52,226
Total liabilities	1,601,547	1,813,939	2,286,581	2,430,637	2,595,854	2,868,113	3,286,787
EQUITY							
Stated Capital	52,188	54,567	58,150	62,948	94,010	105,391	118,117
Statutory Reserves	9,285	10,590	12,080	13,587	15,512	17,792	20,528
Retained Earnings	7,686	9,891	6,790	9,943	18,031	25,327	32,988
Other Reserves	89,596	92,427	131,846	133,993	131,584	145,263	161,681
Total Equity to Equity Owners of the Bank	158,755	167,475	208,865	220,471	259,138	293,773	333,314
Non-Controlling Interest	1,756	2,078	4,107	4,504	6,044	7,868	10,057
Total Equity	160,511	169,553	212,973	224,974	265,183	301,641	343,372
	1,762,058	1,983,491	2,499,554	2,655,612	2,861,036	3,169,754	3,630,159
Adjusted NAVPS	95.2	100.4	125.3	132.2	155.4	165.4	176.2



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