DCB Bank Ltd

BUY

Sector: Banking /Mid-Cap | Earnings Update – 4QFY20

25 May 2020

Background: DCB Bank Limited (formerly Development Credit Bank Limited) has a deposit base of ₹303bn and advances of ₹253bn at the end of 4QFY20, making it the smallest bank in the listed private sector space, including both new and old generation private sector banks. Promoter group the Aga Khan Fund for Economic Development (AKFED) & Platinum Jubilee Investments holds ~15% stake. DCB services entail Corporate Banking - 12%, SME -11%, Agriculture – 21%, Mortgages – 42%. As on 4QFY20, the bank has a network of 336 branches, with ~30% of branches in the Metro cities.

Sensex	30,672
Nifty	9,039
Price	₹ 60
Target Price (12 months)	₹ 80
Recommendation	BUY

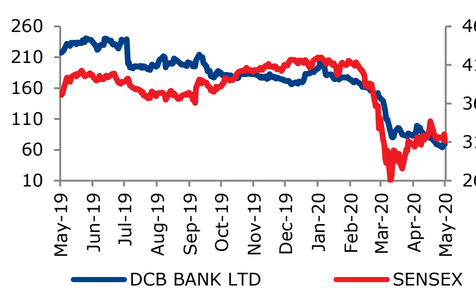
52 Week High/Low	₹ 244.6/60.1
Bloomberg / Reuters	DCBB IN/ DCBA.BO
Equity (shares in mn)	310.4
Mkt. Cap in mn	₹ 18,749.0/ $ 247.3
Avg. Daily Vol. ('000)	1,194.9
Avg. Daily Vol. (mn)	₹ 72.1 /$ 0.9

Shareholding	Mar-19	Dec-19	Mar-20
Promoters (%)	14.9	14.9	14.9
FII (%)	26.0	24.6	22.8
DII (%)	25.1	32.8	35.3
Others (%)	34.0	27.7	27.0
Pledge (% of promoter holding)	0.0	0.0	0.0

Valuation Summary (₹ bn)

Y/E March	2020	2021E	2022E
Net Interest Inc	12.6	13.1	14.7
Other Inc	3.9	3.9	4.0
Pre Prov Profit	7.5	8.1	9.0
PAT	3.4	3.5	4.6
EPS (INR)	10.9	11.2	14.9
EPS growth (%)	3.4	2.8	33.3
PE (X)	5.6	5.4	4.1
P /ABV (X)	0.6	0.5	0.4
Div Yield (%)	-	2.2	2.2
ROA (%)	0.9	0.9	1.0
ROE (%)	9.9	8.7	9.9
Tier – 1 (%)	13.9	13.0	13.00
CAR (%)	17.8	15.9	15.90

Performance(%)	1M	3M	12M
DCB BANK LTD	-15.7	-59.9	-67.9
SENSEX	1.4	-24.6	-16.6



NIM to remain stable though threat of potential slippages and decelerating loan book growth to pressurize near term earnings

- DCB's advances growth slowed to 7.5% YoY (down 0.4% QoQ) to ₹ 253bn in 4QFY20. This was due to the sequential de-growth in the entire portfolio baring Mortgages (42% of the loan book) which increased 2.1% QoQ. Mortgages comprises of Home Loans (38% of Mortgages) and LAP (62%) with average LTV of 49% and 37%, respectively indicating significant equity of customers in their projects. This implies a lesser risk in the book as customers have significant vested interests. The bank continues to see challenges in the CV segment, the recoveries in this segment are highly dependent on economic revival. Overall, the bank has not grown its loan book during the lockdown and the management expects muted growth for 1HFY20 as the economy battles a pandemic that has induced a staggered lockdown. The bank does not view any challenges in HL and LAP portfolio. The challenges continue to be in CV portfolio until economic activity picks up.
- Deposits growth moderated further and stood at ₹303bn (7% YoY, 2% QoQ) CASA deposits witnessed de-growth by 4% YoY (down 6% QoQ) resulting in the CASA ratio to decline by 248bps YoY to 21.5%. The management reiterated their focus on retail term deposits growth, up 14% YoY in 4QFY20. At the end of the quarter, the top 20 depositors constituted 9.07% (as on May 20^{th,} 2020) of the book and the target is to bring it down by reducing the bulk deposit rates in order to discourage growth.
- Cost of funds declined marginally by 8bps QoQ and stood at 7.02% however the yield on advances too declined by 15bps QoQ resulting in a marginal fall in NIM to 3.64%(down 7bps QoQ). The management expects the NIM to remain stable in the near term. However it expects the NIMs to decline if slippages increase over the course of the year.
- Fresh slippages increased by 52% YoY and stood at ₹1.2bn partly due to the conservative approach of the bank on not taking the benefit of Covid 19 for asset classification for the entire March 2020. The NPA for the month of March stood at ₹427mn. Additionally the recoveries plus upgrades stood at ₹713mn (down 46% QoQ). This is explained by the bank's estimate of ₹150mn which the bank was unable to recover/upgrade due to the lockdown enforced in the month of March. Thus resulting in the GNPAs to rise to 2.46% (up 31bps QoQ) from 2.15% in 3QFY20.
- As a result of slippages, provisions doubled QoQ to ₹1.1bn. This has pushed PAT by 30% QoQ to ₹688mn in 4QFY20. Despite an increase in provisions the bank's margin of safety lies at a comfortable point at 2.9x in 4QFY20).
- Operating efficiencies led by slower growth in Opex at 3.1% YoY (down 2% sequentially), helped improve the C/I ratio YoY to 51.09% (down by 327bps) vs. 54.36% in 3QFY20. In view of disruptions again in future, the bank plans to continue its growth of fee income through the digital channel The management is keen to keep costs on the lower end for FY21E.through re-allocation of resources and economies of scale.

Valuation: Despite a well-diversified loan portfolio the bank expects the slippages to rise and credit costs to go up marginally in the short term. An increase in credit costs coupled with muted outlook on loan growth is likely to pressure earnings for FY21E. However we expect the asset quality and earnings to revive sharply in FY22 driven by economic recovery and operational efficiency. DCB Bank trades at 0.4x FY22E P/ABV and 4.1x FY22E P/E. We retain the rating on the stock at BUY with a revised target price of ₹80, assigning a FY22E P/ABV of 0.55x.

Risks: Delayed breakeven of branches; slower rise in fee income on account of Covid disruptions, continued pressure on yields going forward, increase in stress in CV segment.

Results Summary 4QFY20

Y/E March (INR bn)	4QFY20	4QFY19	YoY Growth	3QFY20	QoQ Growth
Net Interest Income	3.2	3.0	7.6%	3.2	0.2%
Other Income	1.1	1.0	10.6%	0.9	18.1%
Pre Provisioning Profit	2.1	1.9	14.5%	1.9	11.7%
PAT	0.7	1.0	-28.6%	1.0	-28.9%
Cost / Income (%)	51.1	53.7		54.4	
Gross NPA (%)	2.5	1.8		2.2	
Net NPA (%)	1.2	0.7		1.0	
Prov Coverage ratio (%)	70.8	78.8		72.0	
CAR (%)	50.74	48.79		51.08	

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