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Banking

Q4FY20 result review
and reco change

Target price: Rs130

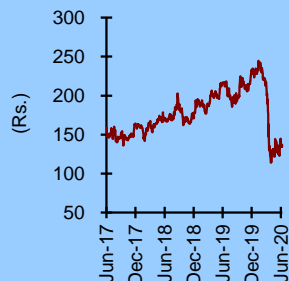
Target price revision
Rs130 from Rs165

Shareholding pattern

	Sep '19	Dec '19	Mar '20
Promoters	0.0	0.0	0.0
Institutional investors	52.9	53.3	52.9
MFs and others	25.6	26.2	27.4
Insurance Cos.	0.0	0.0	0.0
Fls and Banks	3.9	3.9	4.2
FIs	23.4	23.2	21.3
Others	47.2	46.8	47.1

Source: BSE

Price chart



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INDIA

City Union Bank

HOLD

Downgrade from Buy

Consistency broken; return to normalcy will be prolonged **Rs137**

We downgrade City Union Bank (CUBK) to HOLD (from Buy) with a revised target price of Rs130 (earlier: Rs165) after it reported its first quarterly loss, breaking a decade-long consistency in returns and asset quality. Also, near-term triggers for positive surprise are limited, hence current premium multiple (1.7x FY21 P/BV) is likely to re-set lower. While we repose faith in CUBK's SME financing niche coupled with its robust retail liability franchise to manage the crisis effectively, its 10% exposure to vulnerable segments like tourism, hotels, CREs, LRDs, etc. poses risk of near-term volatility in asset quality and earnings. CUBK's Q4FY20 earnings were impacted by higher provision at Rs4.5bn (of which Rs1.25bn or 29bps is towards Covid-related contingency buffer) and muted core business performance with: a) credit growth remaining muted at 4% YoY/flat QoQ; b) margin contraction of 5bps QoQ; c) asset quality deterioration with fresh slippages at Rs4.8bn (>5% run rate).

- ▶ **Asset quality deteriorated; bank expects slippage ratio to remain at 3.25-3.5% in FY21E.** Fresh slippages came in higher at Rs4.8bn (>5% run rate), largely due to lower recovery from SMA accounts in H2-Mar'20 due to lockdown. Similarly, overall recoveries were also lower by Rs0.4bn. As a result, GNPL ratio increased to 4.09% from 3.5% in Q3FY20. GNPL would have been higher by Rs1.25bn (~37bps) if CUBK had not exercised moratorium benefit as per RBI guidelines on those accounts. Management expects the slippage ratio to remain at 3.25-3.5% in FY21 considering its ~10% exposure to vulnerable segments like tourism, hotels, CREs, LRDs, etc.
- ▶ **Loan growth deceleration continues.** Loan growth further moderated to 4% YoY while it was flat QoQ hinting at slowdown in the bank's home state, which contributes 62% of total advances. Management sounded conservative and not very convinced about accelerating growth despite room for market share gain. However, disbursement under CGTMSE scheme is likely to support credit growth in FY21. As per management, ~27% of total loans (Rs93bn) are eligible for CGTMSE scheme implying disbursement of Rs19bn to eligible customers. However, customers opting for refinance under CGTMSE scheme stands at Rs12bn-13bn (~4% of loans), of which Rs8.5bn is already disbursed as at Jun'20.
- ▶ **Strong retail liability franchise likely to support NIM in FY21.** While management expects lower other income in FY21 due to lower ATM fees, lower processing fees, etc. we believe its strong retail liability franchise will support NII progression in FY21E. Its retail liability franchise reflects in <7% contribution from top-20 depositors and only ~11% of total deposits above Rs20mn ticket size. Margins contracted by 5bps QoQ in Q4FY20.
- ▶ **Valuation.** We cut earnings estimate by ~20%/11% for FY21e/22e respectively to factor in higher slippages and higher credit cost. CUBK's premium valuation (2.0x FY20 P/BV) over peer banks was largely due to its decade-long consistency in returns and asset quality. Given its first reported quarterly loss in past 10 years (consistency broken) and lack of visible triggers for early return to historical profitability, a multiple re-set at lower level is likely. Downgrade to **HOLD** with a revised target price of Rs130 (earlier: Rs165).

Market Cap	Rs101bn/US\$1.3bn	Year to Mar	FY19	FY20	FY21E	FY22E
Reuters/Bloomberg	CTBK.BO/CUBK IN	NII (Rs bn)	16.1	16.7	16.9	19.1
Shares Outstanding (mn)	737.3	Net Profit (Rs bn)	6.8	4.8	4.8	7.1
52-week Range (Rs)	244/114	EPS (Rs)	9.8	6.5	6.5	9.6
Free Float (%)	100.0	% Chg YoY	4.3	(33.7)	1.1	46.8
FII (%)	21.3	P/E (x)	14.0	21.1	20.9	14.2
Daily Volume (US\$'000)	2,831	P/BV (x)	2.1	1.9	1.7	1.6
Absolute Return 3m (%)	(16.9)	Net NPA (%)	1.8	1.9	3.1	2.0
Absolute Return 12m (%)	(35.8)	BVPS (Rs/Sh)	66.0	72.0	78.0	87.0
Sensex Return 3m (%)	18.8	RoA (%)	1.6	1.0	0.9	1.3
Sensex Return 12m (%)	(11.5)	RoE (%)	15.2	9.4	8.7	11.6

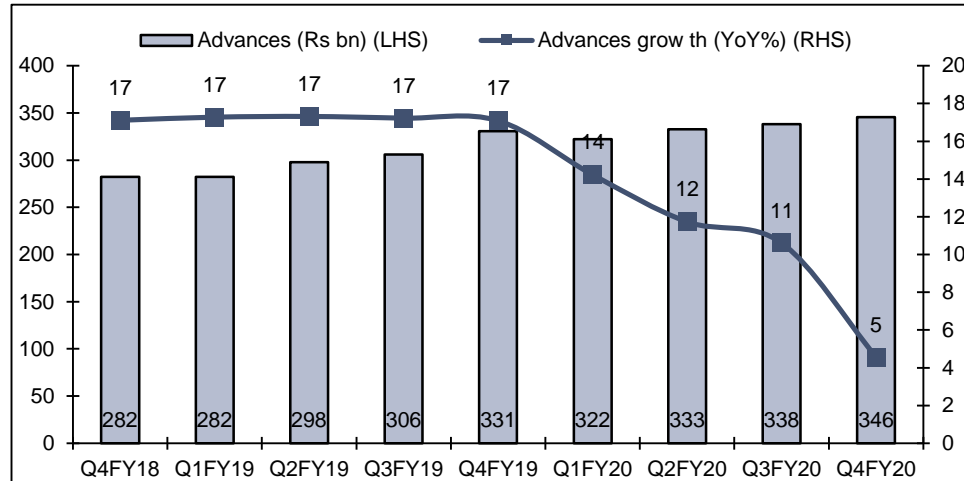
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Table 1: Q4FY20 result review*(Rs mn)*

	Q4FY20	Q4FY19	% change YoY	Q3FY20	% change QoQ
Interest Income	10,417	9,846	5.8	10,609	(1.8)
Interest Expended	6,222	5,640	10.3	6,336	(1.8)
Net interest income (NII)	4,195	4,206	(0.3)	4,273	(1.8)
Other income	1,793	1,469	22.1	1,424	25.9
Total income	5,988	5,675	5.5	5,696	5.1
Operating expenses	2,637	2,297	14.8	2,612	1.0
-Staff expenses	938	914	2.7	1,134	(17.2)
-Other expenses	1,699	1,383	22.8	1,479	14.9
Operating profit	3,351	3,378	(0.8)	3,084	8.6
Total provisions	4,504	907	396.7	810	456.0
Profit before tax	(1,153)	2,471	(146.7)	2,274	(150.7)
Tax	(200)	720	(127.8)	350	(157.1)
Profit after tax	(953)	1,751	(154.4)	1,924	(149.5)
Balance sheet (Rs mn)					
Deposits	4,08,325	3,84,479	6.2	3,98,120	2.6
Advances	3,45,762	3,26,733	5.8	3,38,280	2.2
Gross NPL (Rs mn)	14,134	9,771	44.7	11,854	19.2
Net NPL (Rs mn)	7,785	5,915	31.6	6,494	19.9
Ratios (%)			bps chg	bps chg	
Profitability ratios					
RoaA	(0.8)	1.6	(240)	1.6	(234)
Asset Quality					
Gross NPL ratio	4.1	3.0	114	3.5	59
Net NPL ratio	2.3	1.8	48	2.0	34
Coverage ratio (Cal.)	44.9	39.5	546	45.2	(30)
Business & Other Ratios					
Cost-income ratio	44.0	40.5	356	45.9	(181)
Non int. inc / total income	29.9	25.9	406	25.0	495

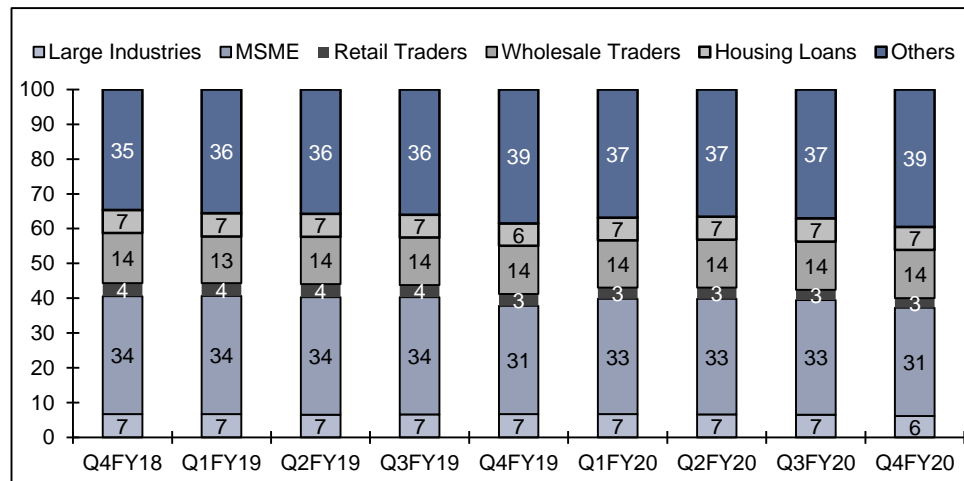
Source: Company, I-Sec research

Chart 1: Credit growth moderated to decadal low at 5% YoY



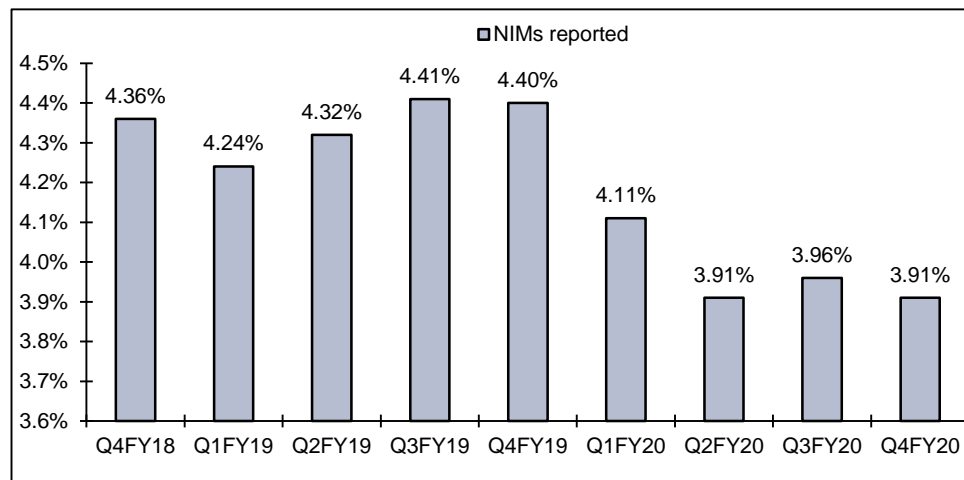
Source: Company, I-Sec research

Chart 2: Loan mix broadly stable: High-yield trading and MSME segments account for ~48% of total advances



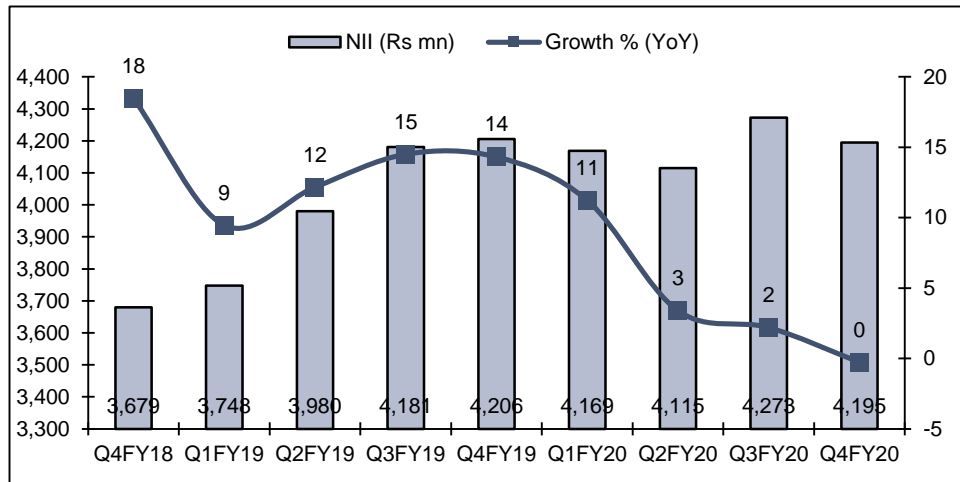
Source: Company, I-Sec research

Chart 3: Margins contracted 5bps QoQ due to fall in C/D ratio



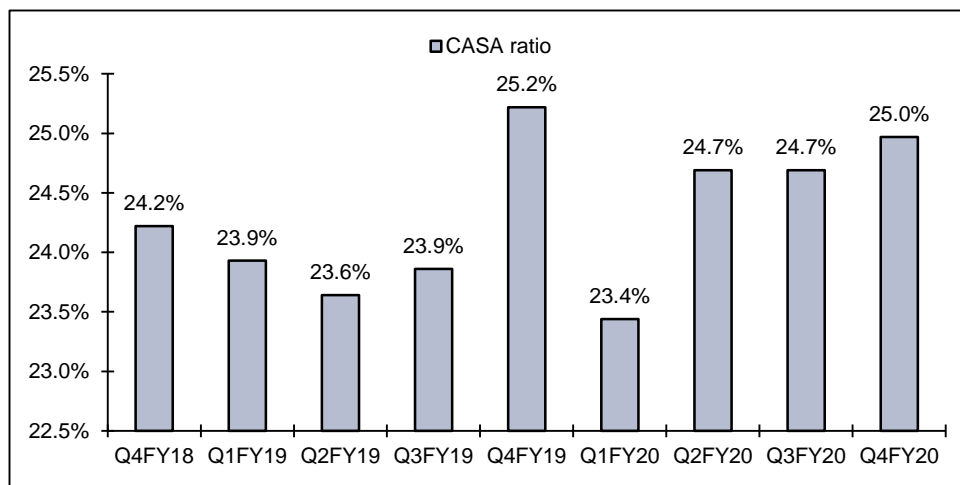
Source: Company, I-Sec research

Chart 4: NII remained flat YoY – lowest in past many quarters



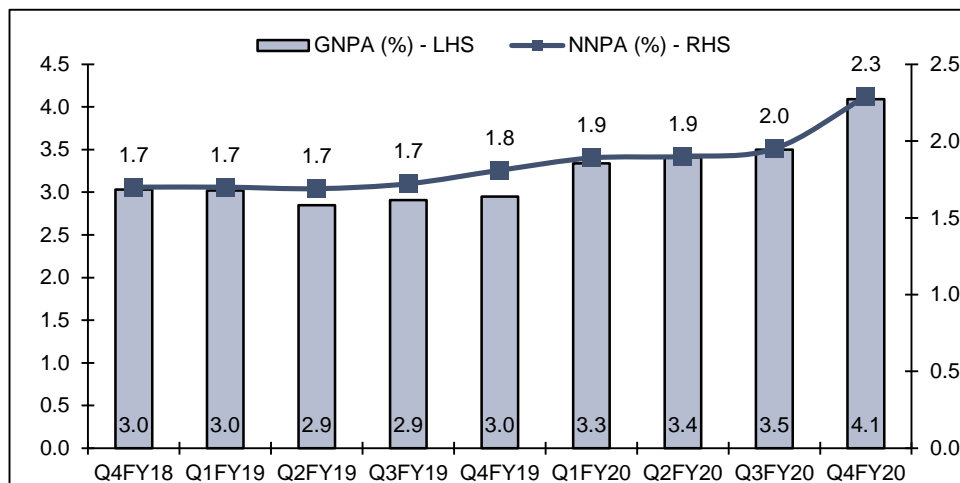
Source: Company, I-Sec research

Chart 5: CASA ratio stood at 25%



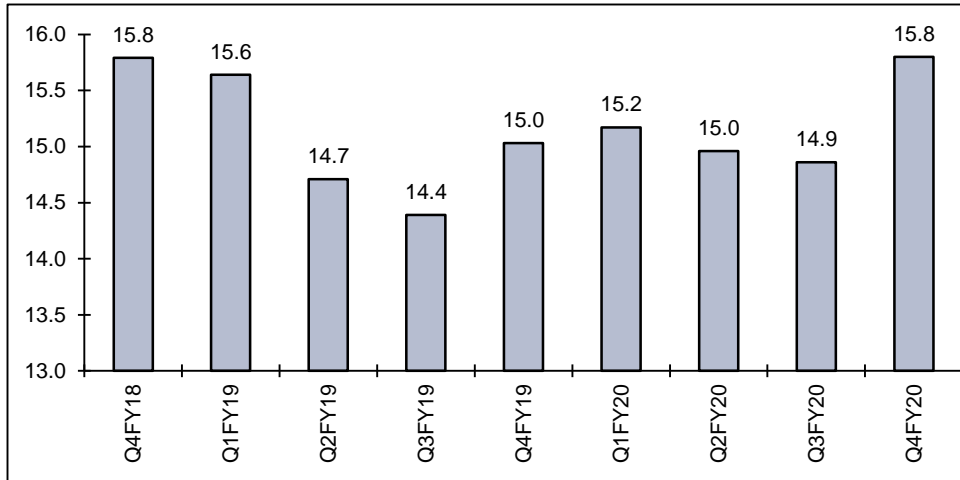
Source: Company, I-Sec research

Chart 6: Asset quality deteriorated



Source: Company, I-Sec research

Chart 7: Tier-1 ratio remained at 15.8%



Source: Company, I-Sec research

Financial summary

Table 2: Profit and loss statement

(Rs mn, year ending March 31)

	FY19	FY20	FY21E	FY22E
Interest Income	37,672	41,686	43,246	47,856
Interest Expense	21,557	24,934	26,361	28,765
Net Interest Income	16,115	16,752	16,885	19,091
% NII Growth	12.7	4.0	0.8	13.1
Treasury Income				
Non-interest income	5,144	6,799	6,375	6,933
Net Revenue	21,259	23,551	23,261	26,024
Employees Expenses	3,644	4,207	4,417	4,947
Other Op. Expenses	5,214	5,931	6,405	7,046
Operating Profit	12,400	13,414	12,439	14,031
% OP Growth	2.7	8.2	-7.3	12.8
Tax	2,420	1,100	1,059	1,554
Total Provisions	3,151	7,551	6,557	5,395
Net Profit	6,829	4,763	4,822	7,082
% PAT Growth	15.3	(30.2)	1.2	46.8

Source: Company data, I-Sec research

Table 3: Balance sheet

(Rs mn, year ending March 31)

	FY19	FY20	FY21E	FY22E
Capital	735	737	737	737
Reserves and Surplus	47,673	52,223	57,046	63,759
Deposits	3,84,479	4,08,325	4,34,866	4,97,922
Borrowings	4,809	20,324	15,180	10,865
Other Liabilities & Provisions	14,893	15,726	16,512	17,338
Total liabilities	4,52,589	4,97,335	5,24,341	5,90,620
Cash & Balances with RBI	19,931	20,304	20,252	22,895
Bal. with banks/ call money	9,702	26,913	22,502	20,351
Investment	77,122	91,168	94,510	1,04,301
Loans and advances	3,26,733	3,39,274	3,66,416	4,21,379
Fixed Assets	2,500	2,452	2,574	2,703
Other Assets	16,600	17,225	18,086	18,990
Total assets	4,52,589	4,97,335	5,24,341	5,90,620
% TA Growth	13	10	5	13

Source: Company data, I-Sec research

Table 4: Key ratios

(Year ending March 31)

	FY19	FY20	FY21E	FY22E
Per Share Data				
Book value per share (INR)	66	72	78	87
Adj. BVPS (INR)	60	64	67	80
Price/Book value	2.1	1.9	1.7	1.6
Price/ Adj. Book value	2.3	2.1	2.0	1.7
EPS(INR)	9.8	6.5	6.5	9.6
P/E Ratio	14.0	21.1	20.9	14.2
DPS	0.5	0.5	-	0.5
Asset Quality				
Gross NPA (Rs mn)	9,771	14,134	20,123	16,933
Gross NPA (%)	2.95	4.09	5.49	4.02
Net NPA (Rs mn)	5,915	7,785	11,037	7,758
Net NPA (%)	1.81	1.95	3.13	1.97
% coverage of NPA	39.5	44.9	45.2	54.2
Delinquencies (%)	2.1	3.3	3.5	2.0

Capital Adequacy Ratios

RWA (Rs mn)	3,14,682	3,26,761	3,52,902	4,05,837
Tier I (%)	15.2	15.9	15.9	15.2
Tier II (%)	0.4	0.4	0.4	0.4
Total CAR (%)	15.6	16.4	16.3	15.7

Business Ratios

Credit / Deposit(%)	85.0	83.1	84.3	84.6
Investment / Deposit (%)	20.1	22.3	21.7	20.9
CASA (%)	25.2	25.0	25.4	25.8
RoaA (%)	1.6	1.0	0.9	1.3
Core RoE (%)	15.2	9.4	8.7	11.6

Earnings Ratios

Interest Inc. / Avg. assets (%)	8.8	8.8	8.5	8.6
Interest Exp./ Avg. assets (%)	5.1	5.2	5.2	5.2
NIM (%)	3.8	3.5	3.3	3.4
Int. exp/ Int earned (%)	57.2	59.8	61.0	60.1
Oth. Inc./ Tot. Inc. (%)	24.2	28.9	27.4	26.6
Staff exp/Total opt. exp (%)	41.1	41.5	40.8	41.2
Cost/ Income Ratio (%)	41.7	43.0	46.5	46.1
Prov./ Operating Profit (%)	25.4	56.3	52.7	38.5

Loan loss prov./Avg. loans

(bps)	104.1	226.7	185.8	137.0
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Source: Company data, I-Sec research

Table 5: RoA tree

(% , year ending March 31)

	FY19	FY20	FY21E	FY22E
Interest income/Assets	8.8	8.8	8.5	8.6
Interest expenses/Assets	5.1	5.2	5.2	5.2
Net interest income/Assets	3.8	3.53	3.3	3.4
Other Inc. from operations/Assets	1.2	1.4	1.2	1.2
Total income/Assets	5.0	5.0	4.6	4.7
Total Exp./Assets	2.1	2.1	2.1	2.2
Operating profit/Assets	2.9	2.8	2.4	2.5
Tax/Assets	0.6	0.2	0.2	0.3
Loan loss provisions/Assets	0.7	1.6	1.3	1.0
Net profit/Assets	1.6	1.0	0.9	1.3
Leverage (x)	9.3	9.4	9.1	9.2
Return on Equity	15.0	9.4	8.6	11.6

Source: Company data, I-Sec research

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