

February 12, 2023

Q3FY23 Result Update

☑ Change in Estimates | ☑ Target | ■ Reco

Change in Estimates

	Current		Previous	
	FY24E	FY25E	FY24E	FY25E
Rating	BUY		BUY	
Target Price	190		220	
NII (Rs. m)	24,608	27,874	24,797	28,970
% Chng.	(0.8)	(3.8)		
Op. Profit (Rs. m)	20,268	22,530	20,399	23,761
% Chng.	(0.6)	(5.2)		
EPS (Rs.)	14.5	16.6	15.8	18.5
% Chng.	(8.2)	(10.5)		

Key Financials - Standalone

Y/e Mar	FY22	FY23E	FY24E	FY25E
NII (Rs m)	19,165	22,740	24,608	27,874
Op. Profit (Rs m)	15,953	18,986	20,268	22,530
PAT (Rs m)	7,602	9,825	10,720	12,276
EPS (Rs.)	10.3	13.3	14.5	16.6
Gr. (%)	-	-	-	-
DPS (Rs.)	0.5	1.1	1.0	1.1
Yield (%)	0.3	0.7	0.6	0.7
NIM (%)	3.7	3.8	3.7	3.8
RoAE (%)	12.2	14.0	13.4	13.5
RoAA (%)	1.5	1.5	1.5	1.5
P/BV (x)	1.8	1.6	1.4	1.2
P/ABV (x)	2.2	1.9	1.6	1.4
PE (x)	15.6	12.1	11.0	9.6
CAR (%)	20.9	21.2	21.1	21.1

Key Data

CTBK.BO | CUBK IN

52-W High / Low	Rs.205 / Rs.109
Sensex / Nifty	60,683 / 17,857
Market Cap	Rs.118bn / \$ 1,436m
Shares Outstanding	740m
3M Avg. Daily Value	Rs.620.61m

Shareholding Pattern (%)

Promoter's	-
Foreign	23.74
Domestic Institution	37.73
Public & Others	38.53
Promoter Pledge (Rs bn)	-

Stock Performance (%)

	1M	6M	12M
Absolute	(3.4)	(9.4)	14.4
Relative	(4.3)	(12.2)	11.1

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City Union Bank

Rating: BUY | CMP: Rs160 | TP: Rs190

Weak quarter; medium term return profile intact

Quick Pointers:

- Earnings miss by 10% due to weaker loan growth, NIM and asset quality.
- Bank trimmed its FY23E loan growth guidance from 15-18%.

We cut our FY24/25E earnings by 8%/10% mainly due to rise in provision costs from 105bps to 127bps, since target is to keep PCR at 50% (now 43%). City Union Bank (CUBK) reported PAT of Rs2.2bn (missed PLe by 10%) led by weaker NIM, loan growth and asset quality. NIM was hit by Rs320mn, due to non-recognition of interest subvention (owing to a procedural lapse likely to regularise in Q4). Bank has turned cautious and lowered its previous FY23 loan growth guidance from 15-18%, due to delay in investment cycle. Hence we trim our FY22-25E credit CAGR from 15.0% to 12.4%. GNPA was more (up 29bps QoQ to 4.63%) due to higher slippage ratio, but would normalise to pre-covid levels in FY24E. We reduce our multiple from 2.0x to 1.8x Sep'24 ABV, due to earnings cut and better core performance of peers. While we lower TP to Rs190 from Rs220, we retain 'BUY' rating as RoA of 1.5% is achievable in FY23/24/25E.

- Miss on numbers; both NII/asset quality dragged PAT:** NII was a miss at Rs5.56bn (PLe Rs6.0bn), due to lower loan growth and NIM. Credit growth was +11.8% YoY (PLe 14.2%), while deposits grew 7.0% YoY (PLe 8.3%). CASA ratio dipped QoQ from 31% to 29%. NIM was lower at 4.0% (PLe 4.3%), mainly due to lower yields (one-off Rs320mn). Other income was a beat at Rs2.24bn (PLe Rs1.86bn) largely driven by strong TWO recovery at Rs1.1bn (Rs481mn in Q2). Opex was lower at Rs2.83bn (PLe Rs3.1bn), due to better employee cost. Core PPoP at Rs4.62bn was a tad higher by 2.2%. GNPA rose by 29bps QoQ to 4.63%, due to higher slippages; hence provisions at Rs2.25bn were a miss. NNPA was stable QoQ at 2.7%, implying a QoQ increase in PCR from 39.4% to 43.5%. PAT was lower at Rs2.2bn (PLe Rs2.42bn).
- Bank trimmed its FY23E loan growth guidance:** Management turned circumspect of achieving 15-18% loan growth in FY23, due to delay in investment cycle. For FY24E bank would achieve double digit loan growth. We have trimmed our FY22-25 credit CAGR from 15.0% to 12.4%. Also, slower deposit mobilization would not affect loan growth for next few quarters, as there is excess liquidity of Rs30bn. CUBK can stretch LDR to 90% for a short time post which it may move back towards 85%. NII impact of Rs320mn was due to non-recognition of interest subvention on KCC loans (backed by gold; end use appropriate) owing to procedural lapse (lack of proper documentation). Bank expects to sort out these irregularities in Q4, which would be corroborated by a RBI inspection.
- Asset quality blip:** GNPA miss was mainly due to higher slippages at Rs4.4bn (PLe Rs3.6bn) which included Rs1.5bn, on account of RBI divergence. Bank expects slippage ratio for FY23 to be between 2.5-2.8%, post which it would normalize to 2.0-2.5% in FY24E. Also PCR is targeted to reach 50% (from 43% now) before FY24E end; hence we raise provision costs for FY24/25E from average 105bps to 127bps. Spicejet is doing well as 35% of Rs1bn exposure has been repaid. OTR pool at ~4% is performing better since slippage over last 1 year was only 7% compared to bank guidance of 15-20%.

Exhibit 1: PAT miss of 10% led by lower NII

P&L Statement (Rs m)	Q3FY23	Q3FY22	YoY gr. (%)	Q2FY23	QoQ gr. (%)
Interest Income	12,056	10,352	16.5	11,812	2.1
Interest Expended	6,499	5,453	19.2	6,133	6.0
Net interest income (NII)	5,557	4,900	13.4	5,679	(2.1)
-Treasury income	353	410	(13.9)	455	(22.4)
Other income	2,243	1,600	40.2	1,735	29.3
Total income	7,801	6,500	20.0	7,414	5.2
Operating expenses	2,827	2,804	0.8	2,849	(0.8)
-Staff expenses	1,268	1,338	(5.2)	1,412	(10.2)
-Other expenses	1,559	1,466	6.4	1,437	8.5
Operating profit	4,973	3,696	34.6	4,565	9.0
Core Operating Profit	4,620	3,286	40.6	4,110	12.4
Total provisions	2,245	1,235	81.8	1,050	113.8
Profit before tax	2,728	2,461	10.9	3,515	(22.4)
Tax	550	500	10.0	750	(26.7)
Profit after tax	2,178	1,961	11.1	2,765	(21.2)
Balance Sheet (Rs m)					
Deposits	499,974	467,217	7.0	498,776	0.2
Advances	420,836	376,290	11.8	419,130	0.4
Ratios (%)					
NIM	4.1	3.9	21	4.0	13.2
RoaA	1.8	1.4	47	1.6	27
RoaE	16.8	12.4	437	14.1	271
Asset Quality					
Gross NPL (Rs m)	19,887	19,986	(0.5)	18,618	6.8
Net NPL (Rs m)	11,245	12,959	(13.2)	11,287	(0.4)
Gross NPL ratio	4.63	5.21	(58.3)	4.37	26
Net NPL ratio	2.67	3.44	(77.2)	2.69	(2)
Coverage ratio (Calc)	43.5	35.2	830	39.4	408
Business & Other Ratios					
Low-cost deposit mix	29.2	29.8	(58)	31.3	(208)
Cost-income ratio	36.2	43.1	(689)	38.4	(219)
Non int. inc / total income	28.8	24.6	414	23.4	536
Credit deposit ratio	84.2	80.5	363	84.0	14
CAR	20.5	19.4	108	20.1	39
Tier-I	1.1	1.1	(2)	1.1	1

Source: Company, PL

NII growth was lower at 13.4% YoY, while it declined 2% QoQ due to lower loan growth/NIM.

Employee cost decreased due to no additional leave encashment provisions.

Overall provisioning spiked to Rs2.5bn due to additional provisioning requirement on divergence

NIM to remain range bound between 3.8-4%

Q3FY23 Conference Call Highlights

Assets & Liabilities – Commentary & build-up

- **In Q3FY23, advances grew by 11.8% YoY/0.4% QoQ.** Due to delay in investment cycle, the earlier growth guidance of 15-18% for FY23 would not be met. For FY24, management guides for credit growth to be in double digits, however more clarity would emerge in Q4FY23.
- **Incremental LDR of 85% would be comfortable to maintain growth.** LDR could stretch upto 90% for a period of 2 quarters, longer period is not in the interest of bank.
- Bank has surplus liquidity of around Rs30bn, which would be sufficient to grow the book without incremental deposits.
- **Gold loan constitutes of 25% of overall loan book in Q3FY23.** Management expects gold loan book to grow by 20-25% in next year. ATS of gold loan for non-agri was Rs0.1-0.15mn and Rs0.15 -0.2mn for agri gold loan.
- **In MSMEs, working capital utilization remains low at 75%** (vs pre-covid levels of 85%), hence the sequential growth has been muted at 1.1%. There is an investment demand seen in solar and non-conventional energy.
- Barring gold loans, majority of the book is floating rate linked. 70-75% of TDs are for a period of 1 year and hence repricing takes place after a year.

NIMs/Yields

- **For Q3FY23, bank reported NIM of 3.88%,** management expects the same to be range bound between 3.8-4%. Yield on advances declined to 9.16% in Q3FY23 vs 9.39% in Q2FY23, owing to lower yielding gold loans at 9%.
- **RBI has hiked repo rate by 225bps till Dec'22,** of which bank has passed on rates of 100-150bps. With recent rate hike of 25bps in Feb'23, bank would further hike rates by 15 to 20 bps. Overall, transmission has been 50 to 60% of the increased rates. Further, deposit rate hike is not expected.
- Interest income from gold loan (mainly KCC agri loans) of Rs320mn has not been recognized, as there were procedural lapses in disbursing the loans. Management expects the same to be recovered by next quarter post submission of proper paper work to RBI.
- **Bank has opened 25 new branches in Q3FY23.** Management would focus on opening new branches in rural areas over metro cities.
- **C/I ratio stood at 36.2% in Q3FY23 vs 38.4% in Q2FY22.** The decline was due to increase in interest rates which in turn lowered the requirement for leave encashment in Q3FY23 (as the same was adequately provided in Q1FY23 and Q2FY23). Hence, due to lower leave encashment provisions employee cost declined by 5.2% YoY/10.2% QoQ. Management guides C/I to be ~40%.
- **For FY23, bank expects RoA to be 1.5%** and is expected to be maintained at these levels going forward. ROA would sustain, led by NPA recoveries.

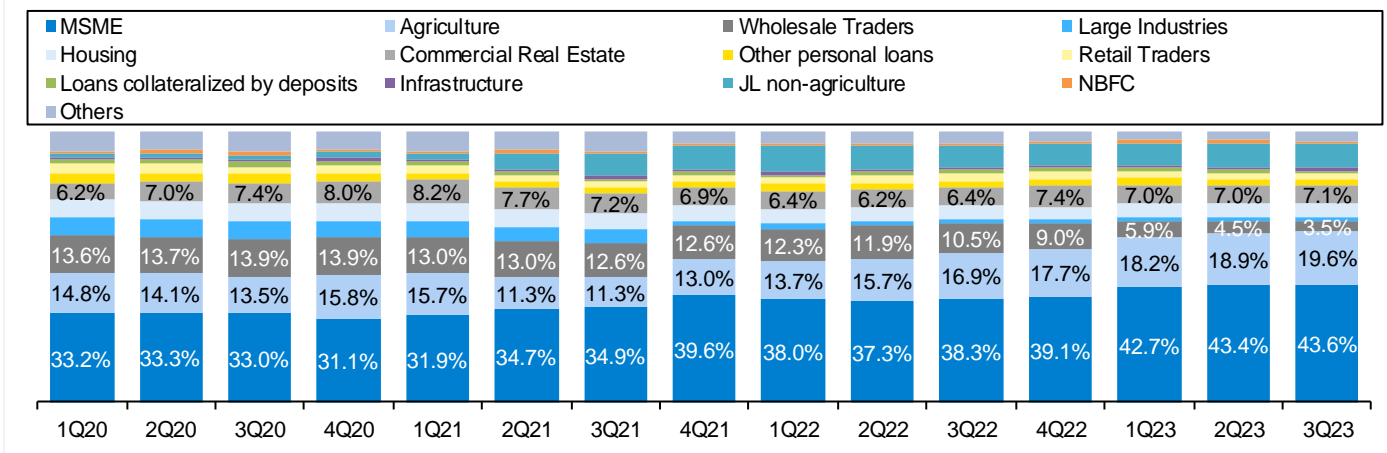
Asset Quality

- **RBI reported divergence in GNPA at RS2.59bn**, mainly due to interpretation issues. Out of these, 13 borrowers whose balance was more than Rs10mn accounted for 89% and balance 11% comprise of 218 borrowers where outstanding was less than 10mn. For these accounts, bank would require an additional provision of Rs400mn.
- **Management plans to shift to ECL regime as per the RBI requirement**, the difference between existing NPA norms and ECL approach is less than Rs1bn. PCR is maintained at 60-70%. After implementation of ECL norms, bank would require an additional provision of Rs2bn, which would be adjusted against CET 1 over a period of 5 years.
- **Bank has been servicing its dues regularly to SpiceJet account**, interest dues have been repaid as per the agreed schedule. Up till now, Rs344mn is repaid and outstanding stands at Rs644mn (final repayment date of June'23). During the quarter, bank wrote back Rs250mn owing to recoveries. Against this account, bank holds a provision of Rs750mn (post the final repayment in June'23, the same would be written back).
- **Slippages increased to Rs4.39bn from Rs2.6bn**, owing to divergence reported by RBI (Rs1.4bn). Hence, management revised the slippages guidance upwards to 2.5-2.8% for FY23. However, expect the same to trend downwards to 2-2.5% from H2FY24.
- **In Q3FY23, there was recovery of Rs1.4bn**, out of which Rs0.73bn was from live account while Rs53bn from technical return of accounts. Management guides to maintain PCR ~50%.

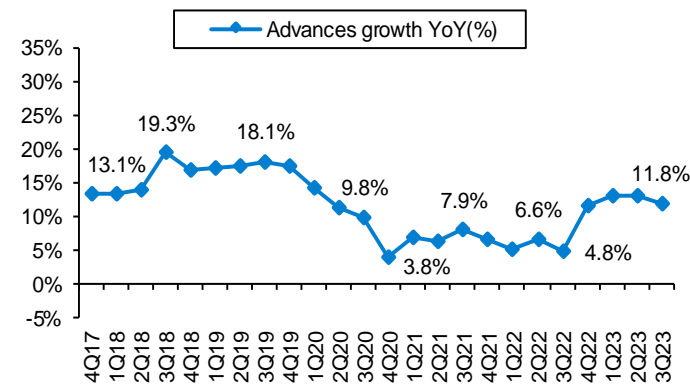
Exhibit 2: MSME growth muted at 1.1% QoQ, overall advances slow too

Advances break-up (Rs m)	Q3FY23	Q3FY22	YoY gr. (%)	Q2FY23	QoQ gr. (%)
MSME	1,87,400	1,47,006	27.5	1,85,427	1.1
Agriculture	84,271	64,755	30.1	80,673	4.5
Wholesale Traders	14,926	40,422	(63.1)	19,017	(21.5)
Large Industries	7,620	6,292	21.1	6,945	9.7
Housing	20,533	19,907	3.1	20,483	0.2
Commercial Real Estate	30,451	24,603	23.8	29,748	2.4
Other personal loans	9,296	8,513	9.2	9,217	0.9
Retail Traders	6,759	10,996	(38.5)	9,063	(25.4)
Loans collateralized by deposits	6,013	6,029	(0.3)	6,379	(5.7)
Infrastructure	3,389	3,032	11.8	3,329	1.8
JL non-agriculture	37,956	30,569	24.2	37,960	(0.0)
NBFC	4,384	3,420	28.2	4,532	(3.3)
Others	17,089	18,327	(6.8)	14,243	20.0
Total Advances	4,30,087	3,83,871	12.0	4,27,016	0.7

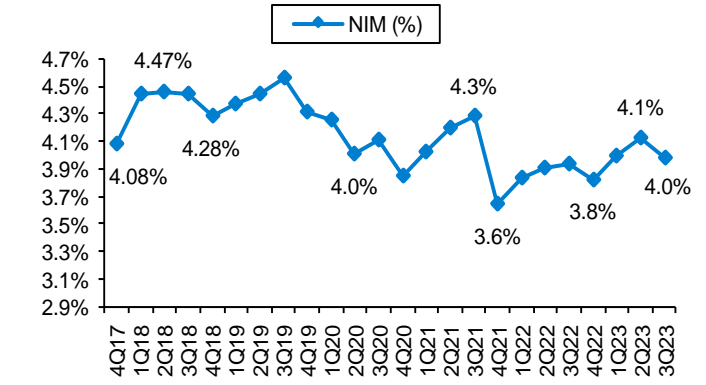
Source: Company, PL

Exhibit 3: MSME continues to maintain dominant share at 43.6%, agri loans share improve to 19.6% led by gold loans


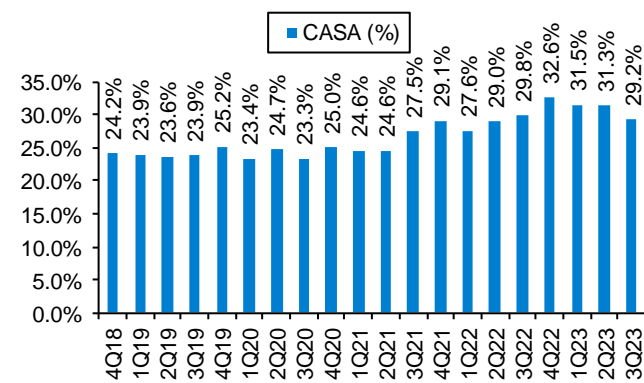
Source: Company, PL

Exhibit 4: MSME and agri drive advance growth to 11.8% YoY


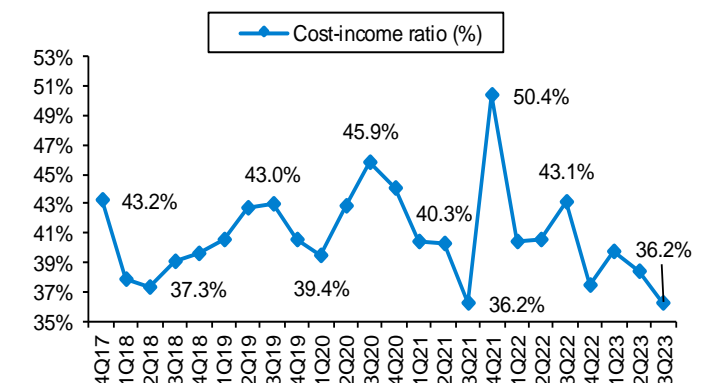
Source: Company, PL

Exhibit 5: NIM declined to 4% owing to lower yields


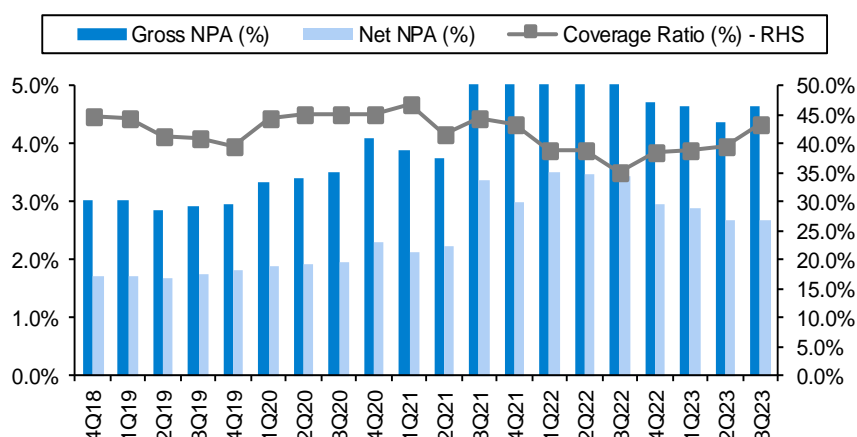
Source: Company, PL

Exhibit 6: CASA decreased to 29%, as TD grows faster


Source: Company, PL

Exhibit 7: C/I to slips to 36% due to lower employee expense


Source: Company, PL

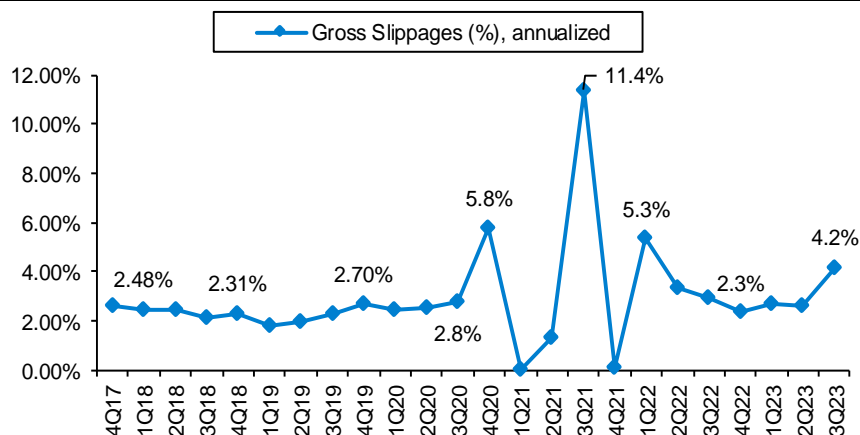
Exhibit 8: GNPA moves up to 4.6%, while PCR inches up to 43.5%


Source: Company, PL

Exhibit 9: Slippages increased to 4.4% due to divergence reported by RBI

Movement of NPL	Q3FY23	Q3FY22	YoY gr. (%)	Q2FY23	QoQ gr. (%)
Opening	18,618	21,193	(12.2)	19,035	(2.2)
Additions	4,391	2,753	59.5	2,615	67.9
Reduction	3,122	3,960	(21.2)	3,032	3.0
Closing	19,887	19,986	(0.5)	18,618	6.8
Slippages (%)	4.41	2.99	141	2.65	176

Source: Company, PL

Exhibit 10: Slippages increased to 4%, expected to normalize from H2FY24


Source: Company, PL

**Exhibit 11: Return ratios are on track to see mid-tier levels**

Du-pont Analysis	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E
NII/Assets	3.6	3.8	3.8	3.5	3.6	3.3	3.5	3.5	3.5
Other inc./Assets	1.4	1.4	1.2	1.4	1.3	1.3	1.2	1.3	1.3
Net revenues/Assets	5.0	5.2	5.0	5.0	4.9	4.7	4.8	4.8	4.8
Opex/Assets	2.1	2.0	2.1	2.1	2.0	1.9	1.8	1.9	2.0
Provisions/Assets	0.9	1.1	0.7	1.6	1.5	1.1	1.0	0.9	0.8
Taxes/Assets	0.6	0.5	0.6	0.2	0.2	0.4	0.4	0.4	0.5
ROA (%)	1.5	1.6	1.6	1.0	1.2	1.3	1.5	1.5	1.5
ROE (%)	14.9	15.1	15.2	9.4	10.6	12.2	14.0	13.4	13.5

Source: Company, PL

Income Statement (Rs. m)

Y/e Mar	FY22	FY23E	FY24E	FY25E
Int. Earned from Adv.	34,540	39,124	48,260	56,741
Int. Earned from invt.	6,305	8,395	10,562	12,077
Others	203	571	480	488
Total Interest Income	41,048	48,090	59,303	69,307
Interest Expenses	21,883	25,350	34,695	41,433
Net Interest Income	19,165	22,740	24,608	27,874
Growth(%)	4.7	18.7	8.2	13.3
Non Interest Income	7,591	7,963	9,400	10,212
Net Total Income	26,756	30,703	34,008	38,086
Growth(%)	0.8	15.2	22.6	15.7
Employee Expenses	5,036	5,458	6,347	7,161
Other Expenses	4,916	6,260	7,394	8,395
Operating Expenses	10,803	11,717	13,741	15,556
Operating Profit	15,953	18,986	20,268	22,530
Growth(%)	8.7	19.0	6.7	11.2
NPA Provision	5,535	6,011	5,779	6,020
Total Provisions	6,101	6,415	6,345	6,586
PBT	9,852	12,571	13,922	15,943
Tax Provision	2,250	2,746	3,202	3,667
Effective tax rate (%)	22.8	21.8	23.0	23.0
PAT	7,602	9,825	10,720	12,276
Growth(%)	28.2	29.2	9.1	14.5

Balance Sheet (Rs. m)

Y/e Mar	FY22	FY23E	FY24E	FY25E
Face value	1	1	1	1
No. of equity shares	740	740	740	740
Equity	740	740	740	740
Networth	65,857	74,995	85,088	96,960
Growth(%)	12.7	13.9	13.5	14.0
Adj. Networth to NNPA's	11,911	11,336	10,274	10,906
Deposits	4,76,897	5,04,621	5,83,730	6,58,772
Growth(%)	7.1	5.8	15.7	12.9
CASA Deposits	1,55,294	1,54,476	1,82,124	2,05,537
% of total deposits	32.6	30.6	31.2	31.2
Total Liabilities	6,15,309	6,62,837	7,50,949	8,41,589
Net Advances	4,03,585	4,47,980	5,06,721	5,73,034
Growth(%)	11.6	11.0	13.1	13.1
Investments	1,22,212	1,44,177	1,57,607	1,77,868
Total Assets	6,15,309	6,73,136	7,50,949	8,41,589
Growth (%)	15.4	9.4	11.6	12.1

Asset Quality

Y/e Mar	FY22	FY23E	FY24E	FY25E
Gross NPAs (Rs m)	19,332	19,887	20,546	21,818
Net NPAs (Rs m)	11,911	11,336	10,274	10,906
Gr. NPAs to Gross Adv.(%)	4.7	4.4	4.0	3.7
Net NPAs to Net Adv. (%)	3.0	2.5	2.0	1.9
NPA Coverage %	38.4	43.0	50.0	50.0

Profitability (%)

Y/e Mar	FY22	FY23E	FY24E	FY25E
NIM	3.7	3.8	3.7	3.8
RoAA	1.5	1.5	1.5	1.5
RoAE	12.2	14.0	13.4	13.5
Tier I	19.8	20.0	20.0	20.0
CRAR	20.9	21.2	21.1	21.1

Source: Company Data, PL Research

Quarterly Financials (Rs. m)

Y/e Mar	Q4FY22	Q1FY23	Q2FY23	Q3FY23
Interest Income	10,499	10,994	11,812	12,056
Interest Expenses	5,493	5,745	6,133	6,499
Net Interest Income	5,007	5,249	5,679	5,557
YoY growth (%)	16.8	17.3	18.7	13.4
CEB	788	850	799	803
Treasury	-	-	-	-
Non Interest Income	2,030	2,175	1,735	2,243
Total Income	12,529	13,170	13,547	14,300
Employee Expenses	1,136	1,327	1,412	1,268
Other expenses	1,502	1,626	1,437	1,559
Operating Expenses	2,638	2,953	2,849	2,827
Operating Profit	4,398	4,471	4,565	4,973
YoY growth (%)	54.5	16.7	12.7	34.6
Core Operating Profits	3,896	4,262	4,110	4,620
NPA Provision	2,188	1,400	-	2,700
Others Provisions	1,709	1,520	1,050	2,245
Total Provisions	1,709	1,520	1,050	2,245
Profit Before Tax	2,690	2,951	3,515	2,728
Tax	600	700	750	550
PAT	2,090	2,251	2,765	2,178
YoY growth (%)	87.9	30.1	51.8	11.1
Deposits	4,76,897	4,87,721	4,98,776	4,99,974
YoY growth (%)	7.1	9.3	7.7	7.0
Advances	4,03,585	4,01,363	4,19,130	4,20,836
YoY growth (%)	11.6	12.9	12.9	11.8

Key Ratios

Y/e Mar	FY22	FY23E	FY24E	FY25E
CMP (Rs)	160	160	160	160
EPS (Rs)	10.3	13.3	14.5	16.6
Book Value (Rs)	89	101	115	131
Adj. BV (Rs)	73	86	101	116
P/E (x)	15.6	12.1	11.0	9.6
P/BV (x)	1.8	1.6	1.4	1.2
P/ABV (x)	2.2	1.9	1.6	1.4
DPS (Rs)	0.5	1.1	1.0	1.1
Dividend Payout Ratio (%)	18.7	16.9	17.2	19.5
Dividend Yield (%)	0.3	0.7	0.6	0.7

Efficiency

Y/e Mar	FY22	FY23E	FY24E	FY25E
Cost-Income Ratio (%)	40.4	38.2	40.4	40.8
C-D Ratio (%)	84.6	88.8	86.8	87.0
Business per Emp. (Rs m)	164	167	186	205
Profit per Emp. (Rs lacs)	14	17	18	20
Business per Branch (Rs m)	1,211	1,242	1,335	1,421
Profit per Branch (Rs m)	10	13	13	14

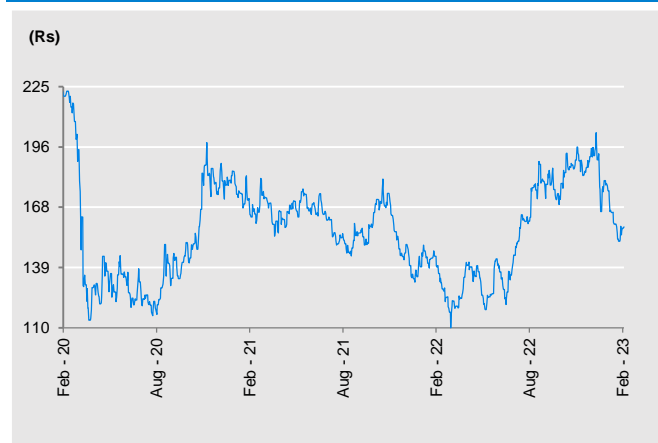
Du-Pont

Y/e Mar	FY22	FY23E	FY24E	FY25E
NII	3.34	3.53	3.46	3.50
Total Income	5.26	5.36	5.55	5.54
Operating Expenses	1.88	1.82	1.93	1.95
PPoP	3.38	3.54	3.62	3.59
Total provisions	1.06	1.00	0.89	0.83
RoAA	1.32	1.53	1.51	1.54
RoAE	12.23	13.95	13.39	13.49

Source: Company Data, PL Research

Price Chart

Recommendation History



No.	Date	Rating	TP (Rs.)	Share Price (Rs.)
1	05-Jan-23	BUY	220	178
2	05-Nov-22	BUY	220	190
3	05-Oct-22	BUY	190	173
4	09-Aug-22	BUY	190	163
5	08-Jul-22	BUY	170	145
6	28-May-22	BUY	170	127
7	09-Apr-22	BUY	180	140

Analyst Coverage Universe

Sr. No.	Company Name	Rating	TP (Rs)	Share Price (Rs)
1	AAVAS Financiers	Accumulate	2,200	1,999
2	Axis Bank	BUY	1,100	933
3	Bank of Baroda	BUY	220	164
4	Can Fin Homes	BUY	700	521
5	City Union Bank	BUY	220	178
6	DCB Bank	BUY	150	114
7	Federal Bank	BUY	175	140
8	HDFC	BUY	3,000	2,613
9	HDFC Bank	BUY	1,850	1,601
10	ICICI Bank	BUY	1,090	870
11	IDFC First Bank	UR	-	60
12	IndusInd Bank	BUY	1,500	1,223
13	Kotak Mahindra Bank	BUY	2,100	1,763
14	LIC Housing Finance	Accumulate	410	376
15	Punjab National Bank	UR	-	57
16	State Bank of India	BUY	730	544

PL's Recommendation Nomenclature (Absolute Performance)

Buy	: > 15%
Accumulate	: 5% to 15%
Hold	: +5% to -5%
Reduce	: -5% to -15%
Sell	: < -15%
Not Rated (NR)	: No specific call on the stock
Under Review (UR)	: Rating likely to change shortly

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