MIRAE ASSET Sharekhan

City Union Bank

Good Q3, RoE to stay low

Stock Update | Result Update

Bank	Sharekhan code: CUB		
Reco/View: Hold ↔	CMP: **Rs. 177**	Price Target: **Rs. 185** ↑	

↑ Upgrade ↔ Maintain ↓ Downgrade

3R MATRIX

	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)		✓	
Right Valuation (RV)		✓	

\+ Positive = Neutral – Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

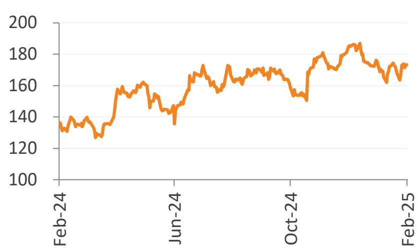
Company details

Market cap:	Rs. 13,108 cr
52-week high/low:	Rs. 188/125
NSE volume: (No of shares)	36.0 lakh
BSE code:	532210
NSE code:	CUB
Free float: (No of shares)	72.0 cr

Shareholding (%)

Promoters	-
FII	27.4
DII	33.6
Others	39.0

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	2.9	0.6	2.9	22.1
Relative to Sensex	2.7	1.9	7.1	12.9

Source: Mirae Asset Sharekhan Research, Bloomberg

Summary

- Earnings grew 13% y-o-y on healthy operating profit growth that was partially offset by higher provisions resulting in RoA/RoE at 1.6%/12.6%.
- Net slippages remained negative for the sixth consecutive quarter as recoveries continued to outpace fresh slippages and thus higher provisions drove up PCR levels.
- Core PPoP growth was strong at 18% y-o-y led by a pick-up in loan growth to 15% y-o-y/ 6% q-o-q, strong fee income, recoveries from W/O accounts and contained opex growth. NIM fell by 9 bps q-o-q. Deposit growth was relatively lower at 11% y-o-y/2% q-o-q resulting in LDR at 87% versus 83% q-o-q.
- Stock trades at 1.5x/1.3x/1.1x its FY2025E/FY2026E/FY2027E ABV. We maintain Hold rating with a revised PT of Rs. 185. Loan growth is unlikely to see further acceleration from current levels, RoE would remain lower at 12-13% in the near term as tailwinds from higher recoveries fade in next two quarters and higher investments are required for scaling up retail business.

Operational performance was healthy led by strong loan growth/ fee income, recoveries from W/O accounts and contained opex growth. Net Interest Income at Rs. 588 crore (marginally below estimates) was up 14% y-o-y/ 1% q-o-q. Yield on advances remained stable q-o-q but cost of funds declined by 12 bps q-o-q driven by rise in cost of deposits resulting in decline in NIMs by 9 bps q-o-q to 3.58%. Core fee income grew 22% y-o-y/7% q-o-q. Treasury gains were reported at Rs. 18 crore versus Rs. 25 crore q-o-q and Rs. 24 crore y-o-y. Other income (ex- trading gains) grew by 27% y-o-y led by higher recoveries from written off accounts. Total operating expenses growth was slower at 10% y-o-y/ flat q-o-q. Operating profit (higher than estimates) grew by 20% y-o-y / 2% q-o-q. The bank reported credit cost at 61 bps of average advances (annualised) versus 59 bps q-o-q resulting in improvement in PCR levels (59% versus 55% q-o-q). Total provisions increased by 63% y-o-y/ 7% q-o-q. PAT at Rs. 286 crore (higher than estimates) grew by 13% y-o-y/ flat q-o-q. Net advances grew 15% y-o-y/6% q-o-q led by MSME loans and gold loans. Deposits grew 11% y-o-y/2% q-o-q. CASA balances grew by 5% y-o-y but declined by 5% q-o-q. CASA ratio at ~27.7% versus 29.1% q-o-q. Term deposits grew by 13% y-o-y/ 4% q-o-q. Slippages were marginally higher at 1.8% annualised versus 1.7% q-o-q, based on trailing 12-month advances. GNPA/NNPA ratios fell 18bps/20bps q-o-q to 3.36%/1.42% and PCR improved to 59% versus 55% q-o-q. Net slippages were negative to the tune of Rs. 20 crore led by higher recoveries. Restructured book stood at Rs. 778 crore (~1.5% of net advances versus 1.8% q-o-q).

Key positives

- Net slippage remained negative for the sixth consecutive quarter as recoveries continued to outpace fresh slippages (1.8% versus 1.7% q-o-q).
- Core operating profits grew 18% y-o-y led by led pick up in loan growth, strong fee income and contained opex growth.

Key Negatives

- CASA deposits fell by 5% q-o-q resulting in muted overall deposit accretion.
- NIMs declined by 9 bps q-o-q.

Management Commentary

- Credit growth is eyed at 12-15% with 2-3% contribution coming from new secured retail products in FY26E. Focus remains on growing core MSME book and accelerating deposit growth. New business would contribute ~8-9% over the next 3-4 years. Credit-deposit ratio is expected to be rangebound at ~85%.
- NIMs likely to sustain at ~3.6% +/-10 bps range and opex growth would be higher due to continued investments in retail business. Cost-to-income ratio will be at 48-50% for the next two years and will start declining once the retail business start delivering meaningfully.
- Credit cost would remain at 60-65 bps going forward. Asset quality outlook remains stable. Endeavor is to bring down the NNPA ratio to ~1.2% by FY25 and shore up PCR levels. Slippages are likely to be lower than recoveries till next two quarters.
- Slippages are expected to be Rs. 200-250 crore in Q4FY25 and around Rs. 700 crore in FY26E. Overall SMA-2 book stands at 1.9% versus 2.0% q-o-q.

Our Call

Valuation – Maintain Hold with a revised PT of Rs. 185 – At CMP, CUB trades at 1.5x/1.3x/1.1x its FY2025E/ FY2026E/ FY2027E ABV. New secured retail businesses would start to contribute meaningfully over the medium term. Loan growth is unlikely to see further acceleration from current levels and RoE trajectory to remain lower at 12-13% in the near term as tailwinds from higher recoveries fades in next two quarters and higher investments are required in scaling up retail business. We acknowledge that the recent improvement in operating performance and better asset quality is encouraging. Execution in expanding new retail business remains a key monitorable.

Key Risks

Stronger loan growth, higher-than-expected margins, contained opex growth and lower credit cost could lead to upside risks.

Valuation (Standalone) Rs cr

Particulars	FY23	FY24	FY25E	FY26E	FY27E
NII	2,163	2,123	2,342	2,650	3,027
PAT	937	1,016	1,134	1,220	1,366
EPS (Rs.)	12.7	13.7	15.3	16.5	18.4
P/E (x)	14.0	12.9	11.6	10.8	9.6
P/BV (x)	2.0	1.7	1.5	1.3	1.1
RoE (%)	13.4	12.8	12.6	12.0	11.9
RoA (%)	1.5	1.5	1.5	1.5	1.5

Source: Company; Mirae Asset Sharekhan estimates

Results | Rs cr

Particulars	Q3FY25	Q3FY24	Q2FY25	y-o-y %	q-o-q %
Interest Income	1,479	1,326	1,434	11%	3%
Interest Expenses	891	810	851	10%	5%
Net Interest Income	**588**	**516**	**582**	**14%**	**1%**
NIM (%)	3.58	3.50	3.67		
Core fee income	111	91	105	22%	7%
Other Income	117	102	122	15%	-4%
Net Operating Revenue	**816**	**709**	**809**	**15%**	**1%**
Employee Expenses	179	156	184	15%	-3%
Other Opex	202	189	197	7%	2%
Total Opex	**380**	**345**	**381**	**10%**	**0%**
Cost to Income Ratio (%)	**46.6%**	**48.6%**	**47.1%**		
Pre Provision Profits	**436**	**364**	**428**	**20%**	**2%**
Provisions & Contingencies - Total	75	46	70	63%	7%
Profit Before Tax	361	318	358	14%	1%
Tax	75	65	73	15%	3%
Effective Tax Rate (%)	20.8	20.4	20.4		
Reported Profits	**286**	**253**	**285**	**13%**	**0%**
Basic EPS	3.9	3.4	3.9	13%	0%
Diluted EPS	3.8	3.4	3.8		
RoA (%)	1.6	1.5	1.6		
Advances	50,409	44,017	47,771	15%	6%
Deposits	58,271	52,726	57,369	11%	2%
Gross NPA	1,693	1,968	1,726	-14%	-2%
Gross NPA Ratio (%)	3.36	4.47	3.54		
PCR - (%)	58.6	52.2	55.1		
Net NPA	702	941	775	-25%	-9%
Net NPAs Ratio (%)	1.42	2.19	1.62		

Source: Company; Mirae Asset Sharekhan Research

Outlook and Valuation

■ **Sector Outlook – Deposit mobilisation and asset quality to be in focus**

System credit growth is slowing and has declined to ~11.5% y-o-y from 16.4% in FY2024 as per the latest fortnight data, mainly driven by slower deposit growth, slowdown in unsecured retail segment and a high credit-deposit ratio. Deposit growth at 10.8% has again started to lag loan growth. However, deposit growth continues to remain rangebound at 10-12% and is mainly led by time deposits rather than CASA. Margins are expected to be under pressure due to higher cost of term deposits, while a reversal in the rate cycle should further lead to yield pressure. Overall, asset quality outlook is stable to positive for the sector, except for the unsecured retail loans and MFI segment. We believe that banks with a robust capital base, strong asset quality, and healthy retail deposit franchises are well-placed to capture growth opportunities

■ **Company Outlook – ROE to remain lower**

New secured retail businesses would start to contribute meaningfully in the medium term. RoE trajectory to remain lower at 12-13% in the near term given tailwind from higher recoveries fade in the next two quarters and higher investments are required in scaling up the retail business. Key monitorable remains execution in scaling up in newer business.

■ **Valuation – Maintain Hold with a revised PT of Rs. 185**

At CMP, CUB trades at 1.5x/1.3x/1.1x its FY2025E/FY2026E/ FY2027E ABV. New secured retail businesses would start to contribute meaningfully over the medium term. Loan growth is unlikely to see further acceleration from current levels and RoE trajectory to remain lower at 12-13% in the near term as tailwinds from higher recoveries fades in next two quarters and higher investments are required in scaling up retail business. We acknowledge that the recent improvement in operating performance and better asset quality is encouraging. Execution in expanding new retail business remains a key monitorable.

About the company

CUB was founded in October 1904 and is headquartered at Kumbakonam, Tamil Nadu, India. The bank mainly focuses on lending to MSME and retail/wholesale trade with a granular asset profile, including providing short-term and long-term loans to the agricultural sector. The bank has 822 branches, of which ~65% are in Tamil Nadu with ~73% business coming from Tamil Nadu. The bank focuses on the niche segment of working capital financing to MSMEs and traders now foraying into secured retail segment. The bank has a comfortable capital position with CRAR of 22.26%, of which Tier-1 constitutes 21.29%.

Investment theme

New secured retail businesses would start to contribute meaningfully in the medium term. RoE trajectory to remain lower at 12-13% in the near term given tailwind from higher recoveries fades in next two quarter and higher investments are required in scaling up retail business. Key monitorable remains execution in scaling up in newer business..

Key Risks

Stronger loan growth, higher-than-expected margins, contained opex and lower credit cost could lead to upside risks.

Additional Data

Key management personnel

Dr. N. Kamakodi	MD & CEO
R Vijay Anandh	ED

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	SBI Funds Management Ltd	8.13
2	HDFC Asset Management Co Ltd	6.09
3	Capital Group Cos Inc/The	5.59
4	Franklin Resources Inc	5.10
5	FundRock Management Co SA	4.62
6	Axis Asset Management Co Ltd/India	2.61
7	HDFC Life Insurance Co Ltd	2.20
8	ICICI Prudential Asset Management	2.06
9	G Visalam	2.04
10	Vaidyanathan Vilasini	2.04

Source: Bloomberg

Understanding the Mirae Asset Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/ weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Mirae Asset Sharekhan Research

MIRAE ASSET Sharekhan

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