

City Union Bank

Sector: Banks /Small-Cap | Earnings Update – 2QFY19

BUY

5 November 2018

Background: City Union Bank (CUB) among the smaller-sized banks in the private sector space operates a network of 607 branches. With about 2/3rds of its branches located in Tamil Nadu the bank's business is largely skewed towards the Southern India. Majority of its business comes from branches located in South India. CUB has a significant chunk of its branches in urban and semi-urban areas. With no identifiable promoters CUB is run by a team of professionals. A slew of FIIs hold a 27.3% equity stake.

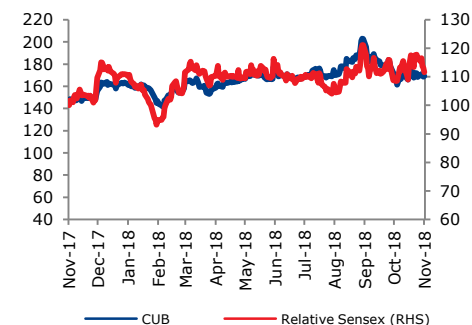
Sensex	34,960
Nifty	10,528
Price	INR 168
Target Price	INR 205
Recommendation	BUY
52 Week High/Low	INR 207/134
Bloomberg / Reuters	CUBK IN / CTBK.BO
Equity (shares in mn)	731.89
Mkt. Cap in bn	INR 122.63/ \$ 1.68
Avg. Daily Vol. ('000)	779.64
Avg. Daily Vol. (mn)	INR 130.63 / \$ 1.79

Shareholding	Sep 17	Jun 18	Sep 18
Promoters (%)	0.00	0.00	0.00
FII (%)	34.15	28.25	27.31
DII (%)	15.62	23.03	24.46
Others (%)	50.23	48.72	48.23
Pledge (% of promoter holding)	0.00	0.00	0.00

Valuation Summary (INR bn)

Y/E March	2018	2019E	2020E
Net Interest Inc	14.3	17.0	19.5
Other Inc	5.3	5.7	6.4
Pre Prov Profit	12.1	13.9	16.0
PAT	5.9	7.5	8.7
EPS	9.1	10.4	11.9
% growth	9.1	13.9	14.2
PE	18.3	16.1	14.1
P/ ABV	3.0	2.7	2.3
Div Yield (%)	0.2	0.2	0.3
ROA (%)	1.6	1.8	1.9
ROE (%)	15.3	16.5	16.5
CAR (%)	16.2	15.7	14.9

Performance %	1M	3M	12M
CUB	-1.7	-1.0	16.4
Sensex	-4.2	-5.8	4.3



Strong growth in advances; Sequential improvement in NIMs

- During 2QFY19, CUB's loan book grew by 17.3% YoY (beating CSEC estimate of 12.5%) to INR 298bn, driven by growth in, MSME (17.4%YoY), Agriculture (16.7%YoY) and Retail trade segments (21.7%YoY) segments. Wholesale trade and JL Non Agricultural segments also grew by 13.8% and 11.9% YoY respectively. The management has reiterated that it expects an overall growth in loan book of 18-20% by FY19E.
- Bank's loan portfolio mix remains in the same range (sequentially) with major contributors being, MSME (33.8%), Agriculture (14.9%), Wholesale trade (13.6%), Large industries (6.5%) and Housing loan (6.6%) segments. Yield on advances remained unchanged (QoQ), during the quarter at 10.9%. NIMs saw sequential improvement of 8bps, led by a 8bps (QoQ) dip in cost of deposits. The management highlighted that the decline in Cost of deposits came in due to the re-pricing (renewal) of a large chunk of older (more than 2 years) deposits.
- Deposits showed moderate growth of 11.8%YoY (vs. CSEC estimate of 11.6%) to INR 345bn. CASA deposits grew by 15% YoY, predominantly led by surge in savings deposits by 18.6%YoY. Consequently, CASA as a share of deposit went up to 23.6% from 23% in 2QFY18.
- Sequentially, GNPA's in absolute numbers, dipped by 0.4% to INR 8.48bn, led by higher recoveries during the quarter (+11.2% QoQ). GNPA's as a % advances fell by 22bps YoY and 17bps QoQ to 2.85%.
- Fresh slippages this quarter stood at INR 1.36bn (up by 8% QoQ), of which INR 250mn came from two large accounts, and the rest entirely comprised of low ticket sized loans (< INR 100mn). No fresh restructuring was done during the quarter and outstanding restructured balance stood at INR 57mn (0.02% of gross advances). There was no fresh sale to ARC during the quarter.
- The management had in 1QFY19, stated the likely stress from 2 accounts (a company in Paper industry and an Educational Institution), amounting to INR 1.5bn. Of these, the bank had recovered the outstanding dues from the Educational Institution, but the stress from the Paper Company remains (amounting to INR 850mn). Going ahead, the management has guided that fresh slippages would be maintained at 1.75- 2% of gross advances for FY19E.
- Other income fell by 23.6% YoY to INR 1.19bn, owing to lower treasury profits. However, fee income saw a 20% YoY growth and stood at INR 688mn.
- Operating profit declined by 7.5% YoY and stood at INR 2.96bn (-1.2% QoQ), due to higher growth in opex (16.1% YoY), predominantly staffing costs. Consequently, cost/ income spiked by 545bps YoY to 42.7%.
- Lower slippages led to a 47.5% YoY de-growth in provisions (despite a 200bps increase in PCR to 65%), which stood at INR 679mn. Hence, PAT grew by a higher 16.1% YoY(4%QoQ) to INR 1.68bn (higher than CSEC estimate of INR 1.25bn).

Valuation: CUB's well-maintained asset quality coupled with superior margins paint a positive outlook for the bank. The stock is currently trading at a P/ABV of 2.3x of FY20E. We maintain our BUY rating, with a target price of INR 205, implying a P/ABV of 2.8X FY20E.

Risks: Systemic slow down in credit growth, weakness in asset quality led by higher slippages from stressed sectors.

Results Summary 2QFY19

Y/E March (INR bn)	2QFY19	2QFY18	YoY Growth	1QFY19	QoQ Growth
Net Interest Income	3.98	3.55	12.2%	3.75	6.2%
Other Income	1.19	1.55	-23.6%	1.29	-8.2%
Pre Provisioning Profit	2.96	3.20	-7.5%	2.99	-1.2%
PAT	1.68	1.45	16.1%	1.62	4.0%
Cost / Income (%)	42.71	37.26		40.58	
Gross NPA (%)	2.85	3.07		3.02	
Net NPA (%)	1.69	1.76		1.70	
Prov Coverage ratio (%)	65.00	63.00		65.00	
CAR (%)	15.11	15.31		16.06	

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