

**HOLD** City Union Bank

## Earnings/NPA redemption in 2Q, but awaiting growth pickup

BFSI - Banks ▶ Result Update ▶ October 28, 2023

TARGET PRICE (Rs): 152

Notwithstanding the anemic credit growth at 2% YoY/3% QoQ, CUBK reported a strong 27% PAT beat at Rs2.8bn/1.7% RoA, mainly owing to lower LLP, and partly offset by lower other income and higher opex. Margin improved after a long break – up by 7bps QoQ to 3.74% due to better loan/investment yields. Asset quality too improved sharply, with GNPA/NNPA ratio down by 25bps/17bps QoQ to 4.7%/2.3%, respectively. Going forward, Bank expects the growth trajectory to gradually improve, and plans to incrementally focus on retail (organically and via co-lending). Bank has highlighted that the recent RBI annual inspection has been completed, and that it does not require reporting any divergence, which we believe is a huge relief. Additionally, Bank expects recovery trends to improve, which should help it to reduce NNPA to around 1.5-2%.

Factoring-in the strong 2Q beat, including better asset-quality outcome, we revise FY24E/25E earnings upward by 8%/4%, respectively, and expect RoA/RoE of 1.4-1.5%/12% over FY24-26E. We retain HOLD on CUBK, with revised TP of Rs152/share, rolling forward on 1.2x Sep-25E ABV. We believe a meaningful re-rating is conditioned to deliver on growth and sustained asset quality.

## City Union Bank: Financial Snapshot (Standalone)

Y/E March (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Net profit	7,602	9,375	9,755	10,851	12,183
Loan growth (%)	11.6	6.7	10.0	12.0	14.0
NII growth (%)	4.7	12.9	1.0	8.9	11.7
NIM (%)	3.5	3.6	3.3	3.3	3.3
PPOP growth (%)	8.7	14.0	(6.5)	8.5	14.6
Adj. EPS (Rs)	10.3	12.7	13.2	14.7	16.5
Adj. EPS growth (%)	28.0	23.2	4.0	11.2	12.3
Adj. BV (INR)	77.0	90.4	102.4	116.2	131.4
Adj. BVPS growth (%)	12.9	17.5	13.2	13.5	13.1
RoA (%)	1.3	1.5	1.4	1.4	1.5
RoE (%)	12.2	13.4	12.4	12.3	12.4
P/E (x)	13.0	10.5	10.1	9.1	8.1
P/ABV (x)	1.7	1.5	1.3	1.1	1.0

Source: Company, Emkay Research

## Growth drags, but NIM improves a tad QoQ

CUBK continued to report sub-par credit growth at 2% YoY/3% QoQ, mainly due to contraction in the agri loan portfolio and slower growth in the SME/Corporate portfolio. That said, CUBK remains hopeful of steady improvement in credit growth of over 10% in FY24 on account of acceleration in gold, VF and housing loans (via co-lending outside TN). Deposit growth too remains moderate, at 6% YoY/2% QoQ, with CASA slipping a bit to 30%. However, increase in CoF was relatively lower, at 3bps QoQ to 4.6% which, coupled with slight improvement in loan/investment yields, led to a 7bps QoQ improvement in NIM to 3.74%. Going forward, the bank expects NIM to stay rangebound.

## Headline asset quality improves QoQ, but need for shoring-up PCR

After a long time, fresh slippages moderated meaningfully to Rs2.3bn/2.1% of loans which, coupled with higher upgrades, led to a 25bps QoQ reduction in the GNPA ratio to 4.7%. As a result, the GNPA ratio increased to 4.9% in Q1FY24 (up by 54bps QoQ). Bank has highlighted that the recent RBI annual inspection has been completed and that it does not require to report any divergence, which we believe is a big relief. Also, Bank expects recovery trends to improve, which should help it to reduce NNPA to around 1.5-2% from 2.3% in 2Q. However, the specific PCR remains sub-par vs peers at 51%, which we believe the bank needs to shore-up, along with building some contingent buffers.

## Outlook and Valuation

CUBK has long struggled on the growth front and, better late than never, has now hired BCG to revamp its credit machinery. Factoring-in the strong 2Q beat including better asset-quality outcome, we revise earnings for FY24E/25E upward by 8%/4%, respectively, and expect RoA/RoE at 1.4-1.5%/12% over FY24-26E. We retain HOLD on the stock, with revised TP of Rs152/share, rolling forward on 1.2x Sep-25E ABV. We believe a meaningful re-rating is conditioned to deliver on growth and sustained asset quality. **Key risks:** Slower growth, faster CASA cannibalization, higher ECL impact, and MD succession.

Target Price – 12M	Sep-24
Change in TP (%)	2.7
Current Reco.	HOLD
Previous Reco.	HOLD
Upside/(Downside) (%)	13.9
CMP (27-Oct-23) (Rs)	133.4

Stock Data	Ticker
52-week High (Rs)	205
52-week Low (Rs)	120
Shares outstanding (mn)	740.4
Market-cap (Rs bn)	99
Market-cap (USD mn)	1,187
Net-debt, FY24E (Rs mn)	NA
ADTV-3M (mn shares)	5
ADTV-3M (Rs mn)	648.9
ADTV-3M (USD mn)	7.8
Free float (%)	97.0
Nifty-50	19,047
INR/USD	83.2
<b>Shareholding, Sep-23</b>	
Promoters (%)	-
FPIs/MFs (%)	23.7/33.2

## Price Performance

(%)	1M	3M	12M
Absolute	3.5	(0.6)	(29.2)
Rel. to Nifty	7.1	2.6	(34.1)

## 1-Year share price trend (Rs)



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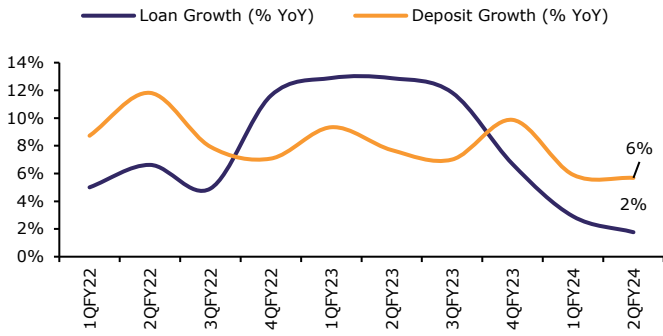
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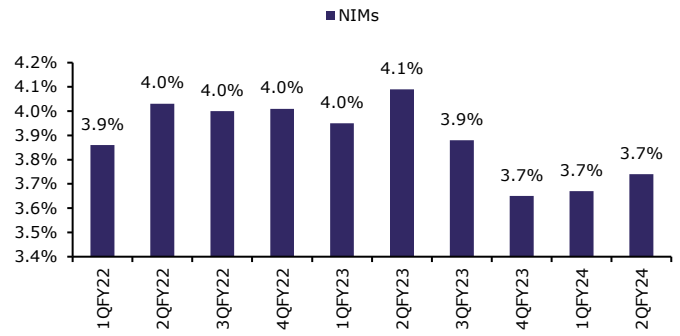
# Story in Charts

**Exhibit 1: Growth remains sub-par vs peers**



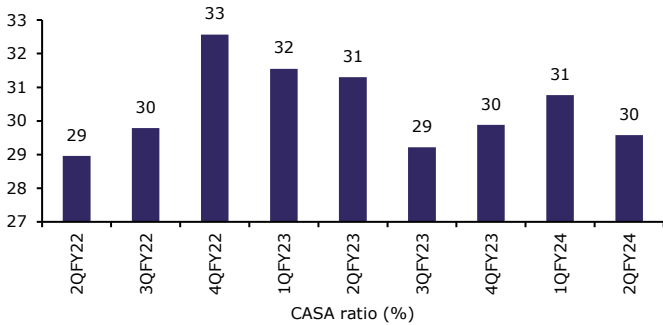
Source: Company, Emkay Research

**Exhibit 2: Margins improve a bit QoQ, after a long break**



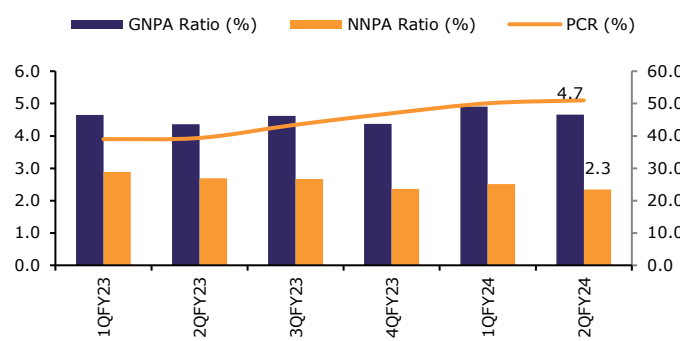
Source: Company, Emkay Research

**Exhibit 3: CASA ratio continues to decelerate**



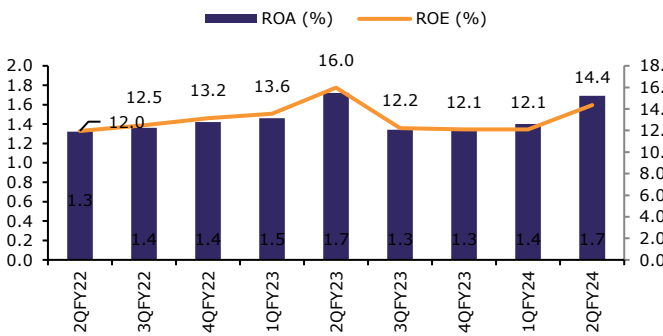
Source: Company, Emkay Research

**Exhibit 4: NPAs trend down due to lower slippages**



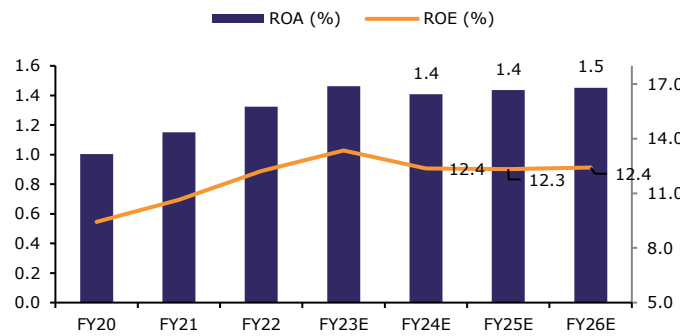
Source: Company, Emkay Research

**Exhibit 5: Lower provisions drive-up RoA to 1.7%**



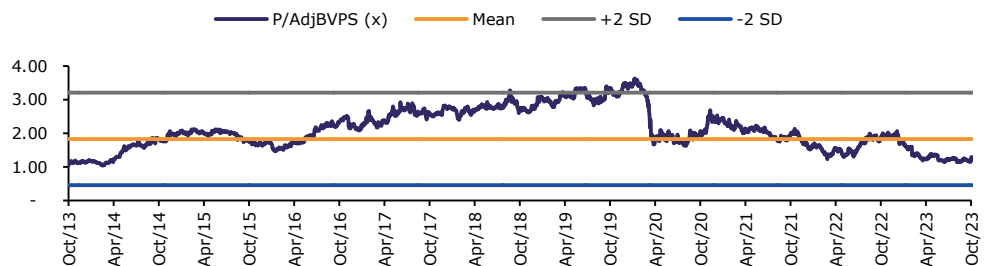
Source: Company, Emkay Research

**Exhibit 6: RoAs to remain range-bound at 1.4-1.5% over FY24-26E**



Source: Company, Emkay Research

**Exhibit 7: The stock has seen a decent de-rating due to frequent regulatory observations and slower growth**



Source: Bloomberg, Emkay Research

**Exhibit 8: Actuals Vs Estimates (Q2FY24)**

(Rs mn)	Actuals	Estimates		Variation		Comments
		Emkay	Consensus	Emkay	Consensus	
Net income	7,205	7,351	7,744	-2%	-7%	Lower other income led to a slight miss
PPOP	3,866	4,200	4,532	-8%	-15%	Higher Staff cost led to a miss
PAT	2,806	2,211	2,476	27%	13%	Lower provisioning led to a beat on PAT

Source: Company, Emkay Research

**Exhibit 9: Quarterly Summary**

(Rs mn)	2QFY23	3QFY23	4QFY23	1QFY24	2QFY24	YoY (%)	QoQ (%)	FY23	FY24E	YoY (%)
Interest Earned	11,812	12,056	12,281	12,662	13,040	10	3	47,143	53,945	14
Interest Exp	6,133	6,499	7,138	7,436	7,656	25	3	25,515	32,100	26
Net Interest Income	5,679	5,557	5,143	5,225	5,384	-5	3	21,628	21,845	1
Global NIMs (reported)	4.09	3.88	3.65	3.67	3.74	-35bps	7bps	3.57	3.33	-25bps
Non-interest Income	1,735	2,243	1,950	1,915	1,821	5	-5	8,104	8,282	2
Operating Expenses	2,849	2,827	2,922	2,998	3,339	17	11	11,552	13,124	14
Pre Provisioning Profit	4,565	4,973	4,170	4,143	3,866	-15	-7	18,180	17,004	-6
Provision & Contingencies	1,050	2,245	1,590	1,520	560	-47	-63	6,405	5,527	-14
PBT	3,515	2,728	2,580	2,623	3,306	-6	26	11,775	11,476	-3
Income Tax Expense (Gain)	750	550	400	350	500	-33	43	2,400	1,721	-28
Net Profit/(Loss)	2,765	2,178	2,180	2,273	2,806	2	23	9,375	9,755	4
Gross NPA (%)	4.36	4.62	4.37	4.91	4.66	30bps	-25bps	4.37	4.10	-27bps
Net NPA (%)	2.69	2.67	2.36	2.51	2.34	-35bps	-17bps	2.36	2.09	-27bps
Deposits (Rs bn)	499	500	524	517	527	6	2	524	572	9
Net Advances (Rs bn)	419	421	431	414	427	2	3	431	474	10

Source: Company, Emkay Research

**Exhibit 10: Revision in Estimates**

Y/E Mar (Rs mn)	FY24E			FY25E			FY26E		
	Earlier	Revised	Change	Earlier	Revised	Change	Earlier	Revised	change
Net income	30,281	30,128	-0.5%	33,425	33,110	-0.9%	38,358	37,504	-2.2%
PPOP	17,567	17,004	-3.2%	19,050	18,446	-3.2%	22,135	21,148	-4.5%
PAT	9,040	9,755	7.9%	10,392	10,851	4.4%	12,011	12,183	1.4%
EPS (Rs)	12.2	13.2	7.9%	14.0	14.7	4.4%	16.2	16.5	1.4%
BV (Rs)	111.4	112.4	0.9%	123.8	125.3	1.3%	138.0	139.8	1.3%

Source: Emkay Research

**Exhibit 11: Key Assumptions**

	FY23A	FY24E	FY25E	FY26E
Loan Growth (%)	6.7	10.0	12.0	14.0
Deposit Growth (%)	9.9	9.2	11.5	12.8
NIM (%)	3.6	3.3	3.3	3.3
GNPA (%)	4.4	4.1	3.7	3.4
Credit Cost (%)	1.5	1.2	1.1	1.1

Source: Emkay Research

## Exhibit 12: Key ratios and trends

(Rs bn)	2QFY22	3QFY22	4QFY22	1QFY23	2QFY23	3QFY23	4QFY23	1QFY24	2QFY24
Loans	371	377	404	402	419	421	431	414	427
Loans – growth YoY (%)	6.6	4.9	11.6	12.9	12.9	11.8	6.7	2.9	1.8
Loans – growth QoQ (%)	4.3	1.5	7.1	(0.4)	4.3	0.6	2.2	(3.9)	3.1
<b>Composition (%)</b>									
- Corporate	24.8	23.6	23.2	19.0	17.3	16.0	16.1	16.3	16.6
- SME/BB	38.2	39.0	39.8	43.5	44.2	44.5	43.8	43.5	42.9
- Retail	23.2	22.1	20.8	20.8	21.1	21.6	22.4	23.7	25.6
- Agri	13.7	15.3	16.1	16.7	17.4	17.9	17.7	16.5	15.0
<b>Liability Profile</b>									
Deposit (Rs bn)	463	467	477	488	499	500	524	517	527
growth YoY (%)	11.8	7.9	7.1	9.3	7.7	7.0	9.9	5.9	5.7
growth QoQ (%)	3.8	0.9	2.1	2.3	2.3	0.2	4.8	(1.4)	2.1
CASA (%)	29.0	29.8	32.6	31.5	31.3	29.2	29.9	30.8	29.6
CA (%)	8.5	8.8	9.7	9.5	8.7	8.0	9.1	9.2	9.0
SA (%)	20.5	21.0	22.9	22.0	22.6	21.2	20.8	21.5	20.5
Branches (No. of)	702	702	727	727	727	752	752	752	752
NIM (%)	4.03	4.00	4.01	3.95	4.09	3.88	3.65	3.67	3.74
<b>Asset Quality</b>									
GNPA (%)	5.6	5.2	4.7	4.7	4.4	4.6	4.4	4.9	4.7
NNPA (%)	3.5	3.4	3.0	2.9	2.7	2.7	2.4	2.5	2.3
PCR (%)	38.9	35.2	38.4	39.0	39.4	43.5	47.0	50.1	51.0
<b>Capital Adequacy (%)</b>									
CAR	19.2	19.4	20.9	20.5	20.1	20.5	22.3	23.0	22.2
<b>ROE Decomposition (%)</b>									
NII	3.7	3.7	3.6	3.6	3.8	3.7	3.3	3.4	3.5
Other Income	1.2	0.9	1.1	1.4	0.9	1.2	1.1	1.0	1.0
Treasury	0.4	0.3	0.4	0.1	0.3	0.2	0.1	0.3	0.2
Opex	2.2	2.1	1.9	2.0	1.9	1.9	1.9	2.0	2.2
PPOP	3.2	2.8	3.2	3.1	3.1	3.3	2.7	2.7	2.5
Provisioning Cost	1.2	0.9	1.2	1.1	0.7	1.5	1.0	1.0	0.4
PBT	2.0	1.9	1.9	2.0	2.4	1.8	1.7	1.7	2.1
ROA	1.4	1.5	1.5	1.6	1.9	1.4	1.4	1.5	1.8
Leverage (x)	8.5	8.5	8.6	8.6	8.6	8.5	8.4	8.1	7.9
ROE	12.1	12.5	12.9	13.4	16.0	12.2	11.9	12.0	14.4

Source: Company, Emkay Research

## City Union Bank: Standalone Financials and Valuations

Profit and Loss					
Y/E March (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Interest Income	41,048	47,143	53,945	57,483	62,036
Interest Expense	21,883	25,515	32,100	33,689	35,448
<b>Net interest income</b>	<b>19,165</b>	<b>21,628</b>	<b>21,845</b>	<b>23,794</b>	<b>26,588</b>
NII growth (%)	4.7	12.9	1.0	8.9	11.7
Other income	7,591	8,104	8,282	9,315	10,916
<b>Total Income</b>	<b>26,756</b>	<b>29,732</b>	<b>30,128</b>	<b>33,110</b>	<b>37,504</b>
Operating expenses	10,803	11,552	13,124	14,664	16,357
<b>PPOP</b>	<b>15,953</b>	<b>18,180</b>	<b>17,004</b>	<b>18,446</b>	<b>21,148</b>
PPOP growth (%)	8.7	14.0	(6.5)	8.5	14.6
<b>Core PPOP</b>	<b>15,332</b>	<b>18,103</b>	<b>16,011</b>	<b>17,156</b>	<b>19,213</b>
Provisions & contingencies	6,102	6,405	5,527	5,213	5,919
<b>PBT</b>	<b>9,852</b>	<b>11,775</b>	<b>11,476</b>	<b>13,233</b>	<b>15,229</b>
Extraordinary items	0	0	0	0	0
Tax expense	2,250	2,400	1,721	2,382	3,046
Minority interest	0	0	0	0	0
Income from JV/Associates	0	0	0	0	0
<b>Reported PAT</b>	<b>7,602</b>	<b>9,375</b>	<b>9,755</b>	<b>10,851</b>	<b>12,183</b>
PAT growth (%)	28.2	23.3	4.1	11.2	12.3
<b>Adjusted PAT</b>	<b>7,602</b>	<b>9,375</b>	<b>9,755</b>	<b>10,851</b>	<b>12,183</b>
<b>Diluted EPS (Rs)</b>	<b>10.2</b>	<b>12.5</b>	<b>13.0</b>	<b>14.5</b>	<b>16.3</b>
Diluted EPS growth (%)	27.7	23.2	4.0	11.2	12.3
<b>DPS (Rs)</b>	<b>1.0</b>	<b>1.0</b>	<b>1.5</b>	<b>1.7</b>	<b>2.0</b>
<b>Dividend payout (%)</b>	<b>9.7</b>	<b>7.9</b>	<b>11.4</b>	<b>11.6</b>	<b>12.2</b>
Effective tax rate (%)	22.8	20.4	15.0	18.0	20.0
Net interest margins (%)	3.5	3.6	3.3	3.3	3.3
Cost-income ratio (%)	40.4	38.9	43.6	44.3	43.6
Shares outstanding (mn)	739.6	740.4	740.4	740.4	740.4

Source: Company, Emkay Research

Asset Quality and Other Metrics					
Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
<b>Asset quality</b>					
Gross NPLs	19,331.1	19,200.9	19,817.4	20,142.3	20,790.5
Net NPLs	11,910.6	10,176.0	9,908.7	9,064.0	8,316.2
GNPA ratio (%)	4.7	4.4	4.1	3.7	3.4
NNPA ratio (%)	3.0	2.4	2.1	1.7	1.4
Provision coverage (%)	38.4	47.0	50.0	55.0	60.0
Gross slippages	12,756.8	13,290.3	12,329.6	10,830.7	12,964.4
Gross slippage ratio (%)	3.5	3.2	2.6	2.0	2.1
LLP ratio (%)	1.6	1.5	1.2	1.1	1.1
NNPA to networth (%)	17.2	13.1	11.5	9.4	7.7
<b>Capital adequacy</b>					
Total CAR (%)	20.9	22.3	22.0	21.9	21.8
Tier-1 (%)	19.8	21.3	21.1	21.1	21.0
CET-1 (%)	19.8	21.3	21.1	21.1	21.0
RWA-to-Total Assets (%)	51.9	50.7	53.0	54.0	54.0
<b>Miscellaneous</b>					
Total income growth (%)	0.8	13.6	12.6	7.3	9.2
Opex growth (%)	2.8	6.9	13.6	11.7	11.5
Core PPOP growth (%)	24.2	18.1	(11.6)	7.1	12.0
PPOP margin (%)	32.8	32.9	27.3	27.6	29.0
PAT/PPOP (%)	47.6	51.6	57.4	58.8	57.6
LLP-to-Core PPOP (%)	39.8	35.4	34.5	30.4	30.8
Yield on advances (%)	9.3	9.4	9.7	9.5	9.2
Cost of funds (%)	4.4	4.6	5.4	5.2	4.9

Source: Company, Emkay Research

Balance Sheet					
Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Share capital	740	740	740	740	740
Reserves & surplus	65,117	73,832	82,476	92,068	1,02,770
<b>Net worth</b>	<b>65,857</b>	<b>74,572</b>	<b>83,216</b>	<b>92,808</b>	<b>1,03,510</b>
Deposits	4,76,897	5,23,979	5,71,945	6,37,443	7,19,110
Borrowings	53,118	46,881	44,537	42,310	40,195
<b>Interest bearing liab.</b>	<b>5,30,015</b>	<b>5,70,860</b>	<b>6,16,482</b>	<b>6,79,753</b>	<b>7,59,304</b>
<b>Other liabilities &amp; prov.</b>	<b>19,437</b>	<b>20,514</b>	<b>20,768</b>	<b>18,454</b>	<b>23,685</b>
<b>Total liabilities &amp; equity</b>	<b>6,15,309</b>	<b>6,65,946</b>	<b>7,20,467</b>	<b>7,91,015</b>	<b>8,86,500</b>
Net advances	4,03,585	4,30,533	4,73,606	5,30,458	6,04,877
Investments	1,22,212	1,43,326	1,51,759	1,60,516	1,75,470
Cash, other balances	66,869	66,493	67,824	71,385	75,940
<b>Interest earning assets</b>	<b>5,92,666</b>	<b>6,40,352</b>	<b>6,93,188</b>	<b>7,62,358</b>	<b>8,56,287</b>
Fixed assets	2,147	2,393	3,118	3,498	3,924
Other assets	20,496	23,200	24,160	25,160	26,289
<b>Total assets</b>	<b>6,15,309</b>	<b>6,65,946</b>	<b>7,20,467</b>	<b>7,91,015</b>	<b>8,86,500</b>
BVPS (Rs)	89.0	100.7	112.4	125.3	139.8
Adj. BVPS (INR)	77.0	90.4	102.4	116.2	131.4
Gross advances	4,11,005	4,39,558	4,83,514	5,41,536	6,17,351
Credit to deposit (%)	84.6	82.2	82.8	83.2	84.1
CASA ratio (%)	32.6	29.9	27.4	27.1	27.6
Cost of deposits (%)	4.6	4.6	5.4	5.2	4.9
Loans-to-Assets (%)	65.6	64.6	65.7	67.1	68.2
Net advances growth (%)	11.6	6.7	10.0	12.0	14.0
Deposit growth (%)	7.1	9.9	9.2	11.5	12.8
Book value growth (%)	12.6	13.1	11.6	11.5	11.5

Source: Company, Emkay Research

Valuations and Key Ratios					
Y/E Mar	FY22	FY23	FY24E	FY25E	FY26E
P/E (x)	13.0	10.5	10.1	9.1	8.1
P/B (x)	1.7	1.5	1.3	1.1	1.0
P/ABV (x)	1.7	1.5	1.3	1.1	1.0
P/PPOP (x)	6.2	5.4	5.8	5.4	4.7
Dividend yield (%)	0.7	0.8	1.1	1.3	1.5
<b>DuPont-RoE split (%)</b>					
NII/avg assets	3.3	3.4	3.2	3.1	3.2
Other income	1.3	1.3	1.2	1.2	1.3
Fee income	0.1	0.1	0.1	0.1	0.1
Opex	1.9	1.8	1.9	1.9	2.0
<b>PPOP</b>	<b>0.7</b>	<b>0.7</b>	<b>0.6</b>	<b>0.6</b>	<b>0.6</b>
Core PPOP	2.7	2.8	2.3	2.3	2.3
Provisions	1.1	1.0	0.8	0.7	0.7
Tax expense	0.4	0.4	0.2	0.3	0.4
<b>RoA (%)</b>	<b>1.3</b>	<b>1.5</b>	<b>1.4</b>	<b>1.4</b>	<b>1.5</b>
Leverage ratio (x)	9.2	9.1	8.8	8.6	8.5
<b>RoE (%)</b>	<b>12.2</b>	<b>13.4</b>	<b>12.4</b>	<b>12.3</b>	<b>12.4</b>
<b>Quarterly data</b>					
Rs mn, Y/E March	Q2FY23	Q3FY23	Q4FY23	Q1FY24	Q2FY24
NII	5,679	5,557	5,143	5,225	5,384
NIM (%)	4.1	3.9	3.7	3.7	3.7
PPOP	4,565	4,973	4,170	4,143	3,866
PAT	2,765	2,178	2,180	2,273	2,806
EPS (Rs)	3.74	2.95	2.94	3.07	3.79

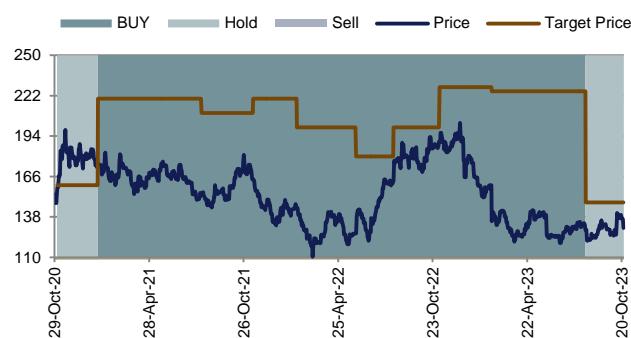
Source: Company, Emkay Research

**RECOMMENDATION HISTORY - DETAILS**

Date	CMP (INR)	TP (INR)	Rating	Analyst
12-Oct-23	140	148	Hold	Anand Dama
12-Aug-23	129	148	Hold	Anand Dama
09-Mar-23	140	225	Buy	Anand Dama
13-Feb-23	135	225	Buy	Anand Dama
05-Nov-22	190	228	Buy	Anand Dama
09-Aug-22	163	200	Buy	Anand Dama
29-May-22	127	180	Buy	Anand Dama
05-Feb-22	144	200	Buy	Anand Dama
13-Nov-21	164	220	Buy	Anand Dama
06-Aug-21	153	210	Buy	Anand Dama
28-May-21	174	220	Buy	Anand Dama
04-Feb-21	176	220	Buy	Anand Dama
20-Jan-21	175	220	Buy	Anand Dama
03-Nov-20	158	160	Hold	Anand Dama

Source: Company, Emkay Research

**RECOMMENDATION HISTORY - TREND**



Source: Company, Bloomberg, Emkay Research

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