

**Squeezed Margins & Macro Slowdown hitting core business**

**CMP: Rs 227**

**Rating: NEUTRAL**

**Target Price: Rs 221**

**Stock Info**

BSE	532648
NSE	CUB
Bloomberg	CUBK IN
Reuters	CTBK.BO
Sector	Banks
Face Value (Rs)	1
Equity Capital (Rs Cr)	73
Mkt Cap (Rs Cr)	16,839
52w H/L (Rs)	175 / 249
Avg Yearly Vol (in 000')	768

**Shareholding Pattern %**

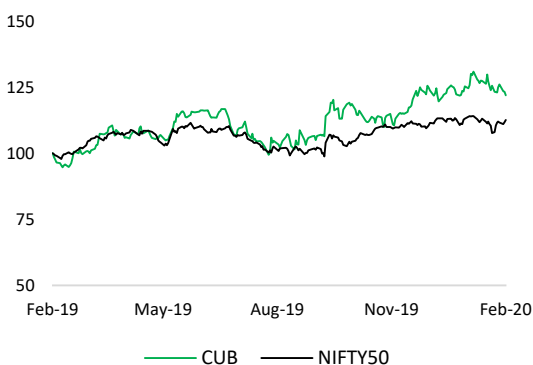
(As on Dec, 2019)

Promoters	0.0
FII	22.63
DII	30.62
Public & Others	46.75

**Stock Performance (%)**

	3m	6m	12m
CUB	7.2	17.7	22.9
Nifty	3.0	11.7	12.6

**CUB Vs Nifty**



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*City Union Bank (CUB) reported mixed set of numbers during Q3FY20. Moderation in loan growth and decline in NIM led to muted NII growth of 2.2% YoY to Rs 427 Cr. Operating Profit grew by +0.5% YoY/ down 11% QoQ at Rs 308 Cr while PAT increased 8.0% YoY/down -0.6% QoQ standing at Rs 192 Cr. Advances growth was moderated to 10.4% YoY/1.6% QoQ. Decline in yield on advances, rising cost of funds and lower investment yields led to compression in NIM to 3.96% vs. 4.41% last year. Slippages elevated due to a Paper company account slippage of Rs 71 Cr taking the slippage ratio to 2.72% for Q3FY20. Asset quality of the bank deteriorated further with GNPA/NNPA at 3.50%/1.95% vs. 3.41%/1.90% sequentially. We downgrade our rating to Neutral with revised target price of Rs 221.*

**Q3FY20 Result Highlights**

**Loan growth moderated further as macro-economic scenario worsened**  
CUB's loan growth was further moderated to 10.4% YoY from 12% YoY in previous quarter mainly due to lower growth in MSME and Agri portfolio. Deposit mobilization worsened with sequential fall by 1.6% QoQ.

**Yields came down while costs went up sequentially**

The Yield on advances came down to 10.73% with the cost of funds going up to 5.18% in Q3FY20. This has put the spreads of the bank under more pressure with CASA ratio stable at 23.3% and cost of deposits at 6.7%.

**Asset Quality deteriorated further**

CUB's asset quality degraded in the quarter with GNPA/NNPA standing at 3.50%/1.95% against last quarter's 3.41%/1.90%. Slippages increased to Rs 229 Cr against Rs 200 Cr in Q2FY20, with a Paper company making up Rs 71 Cr in that.

**High dependence on MSME segment**

CUB's loan book comprised of MSME segment with 33% of the loan mix along with agricultural segment making up 14%. Despite all government policies, both the segments have been a cause of concern among the bankers across the nation due to the unstable nature of the repayment from the asset.

**Management Commentary**

- Management admitted of macroeconomic slowdown hitting business
- Slippages spiked to 2.72% in Q3FY20; SMA 2 at 6% of total loan book
- NPA recovery of Rs 150 Cr during Q3FY20
- Auto sector downturn affecting business hardest
- Expects around Rs 63 Cr of benefit from tax rate cut for the year

**Valuation**

**CUB's Q3FY20 performance was operationally muted with high reliance on MSME segment during times when not everything is going well with the sector. The management has shown huge resilience sacrificing growth against quality borrowers as the economic slowdown has marred all sectors. We cut our loan growth estimate to 13%/15% for FY20/21E from 17% earlier. We expect CUB to report RoAs of ~1.5% and RoE of ~14% in FY21E. We downgrade our rating on the stock to 'NEUTRAL' with a revised target price of Rs 221 based on P/Adj. BV multiple of 2.8 (x) to its FY21E Adj. BV of Rs 79.**

## Q3 FY20 - Quarterly Performance (Standalone)

Income Statement (Rs. in Crore)	Q3 FY20	Q3 FY19	YoY	Q2FY20	QoQ
Interest earned	1061	967	9.7%	1037	2.3%
Interest expended	634	549	15.5%	625	1.3%
<b>NII</b>	<b>427</b>	<b>418</b>	<b>2.2%</b>	<b>412</b>	<b>3.8%</b>
NIM (%)	3.96	4.41	-45bps	3.91	5bps
Non-interest income	142	120	18.8%	195	-27.0%
Operating Expenses	261	231	13.0%	260	0.4%
Employee cost	113.4	92.7	22.2%	113.1	0.2%
Cost-Income ratio (%)	45.9	43.0	289bps	42.9	298bps
<b>Operating Profit</b>	<b>308</b>	<b>307</b>	<b>0.5%</b>	<b>346</b>	<b>-11.0%</b>
Provisions	81	79	2.9%	108	-25.0%
PBT	227	228	-0.3%	239	-4.6%
Tax provisions	35	50	-30.0%	45	-22.2%
Effective tax rate	15%	22%		19%	
<b>Net profit</b>	<b>192</b>	<b>178</b>	<b>8.0%</b>	<b>194</b>	<b>-0.6%</b>
EPS	2.6	2.4	7.7%	2.6	

Asset Quality	Q3 FY20	Q3 FY19	YoY	Q2FY20	QoQ
GNPA	3.50	2.91	59bps	3.41	9bps
NNPA	1.95	1.74	21bps	1.90	5bps
PCR	65.0	65.0	0bps	65.0	0bps

Balance Sheet Positions	Q3 FY20	Q3 FY19	YoY	Q2FY20	QoQ
Advances	33828	30637	10%	33279	1.6%
Deposits	39812	35504	12%	40451	-1.6%
CASA	9294	8470	9.7%	9988	-6.9%
CASA %	23.3	23.9	-51bps	24.7	-135bps
C-D ratio %	85.0	86.3	-132bps	82.3	270bps
Capital Adequacy %	15.5	14.8	70bps	15.5	0bps

Source: Arihant Research, Company Filings, Ace Equity, Bloomberg

## Key Financials

Income Statement (Rs Cr)	2019	2020E	2021E
Interest Earned	3767	4574	5168
Interest Expended	2156	2763	3158
<b>Net Interest Income</b>	<b>1611</b>	<b>1811</b>	<b>2011</b>
Other Income	514	608	690
Fee Income	294	338	388
Treasury Income	87	155	187
<b>Operating Income</b>	<b>2126</b>	<b>2419</b>	<b>2701</b>
Operating Expenses	886	1030	1127
Employee Expenses	364	435	449
<b>Profit before provision &amp; tax</b>	<b>1240</b>	<b>1389</b>	<b>1574</b>
Provisions and Contingencies	315	424	484
<b>Profit Before Tax</b>	<b>925</b>	<b>965</b>	<b>1091</b>
Provision for tax	242	203	229
Exceptional Items	0	0	0
<b>Profit After Tax</b>	<b>683</b>	<b>763</b>	<b>862</b>

Balance Sheet (Rs Cr)	2019	2020E	2021E
<b>Sources of funds</b>			
Share Capital	73	73	73
Total Reserves	4767	5530	6392
<b>Shareholder's Fund</b>	<b>4841</b>	<b>5604</b>	<b>6465</b>
Deposits	38448	43677	50040
Borrowings	481	683	970
Other Liabilities & provision	1489	1718	2039
<b>Total Liabilities</b>	<b>45259</b>	<b>51681</b>	<b>59515</b>
<b>Application of Funds</b>			
Cash & Bank	2963	3220	3592
Investments	7712	9502	11272
Advances	32673	36921	42459
Fixed Assets	250	263	276
Other Assets	1660	1776	1917
<b>Total Assets</b>	<b>45259</b>	<b>51681</b>	<b>59515</b>

Operational Ratios (%)	2019	2020E	2021E
<b>Asset Quality</b>			
Gross NPA	2.96	3.13	3.11
Net NPA	1.81	1.76	1.54
PCR	63.0	64.0	64.0
<b>Growth</b>			
Advances Growth	17.3	13.0	15.0
Deposit growth	17.0	13.6	14.6
Net Profit Growth	15.3	11.7	13.0
<b>Liquidity</b>			
C-D Ratio	85.0	84.5	84.8
CASA	25.2	26.3	27.9
Capital Adequacy	16.1	15.9	16.0
<b>Efficiency</b>			
Cost Income Ratio	41.7	42.6	41.7
Operating Costs to Assets	2.0	2.0	1.9

Valuation Ratios (%)	2019	2020E	2021E
<b>Spread Analysis</b>			
Yield on Advances	10.5	11.5	11.3
Yield on Investments	7.1	6.0	6.0
Cost of Funds	5.9	6.6	6.6
Cost of Deposits	5.9	6.6	6.6
NIM	3.9	3.9	3.8
Interest Spread	4.6	4.9	4.7
<b>Profitability</b>			
ROE	15.2	14.6	14.3
Earnings Per Share (Rs)	9.3	10.4	11.7
Dividend Per Share (Rs)	0.3	0.4	0.4
Adjusted Book Value (Rs)	57.9	67.4	79.1
<b>Valuation</b>			
P / EPS (x)	22.9	20.5	18.2
P / ABV (x)	3.7	3.2	2.7

Source: Arianth Research, Company Filings, Ace Equity, Bloomberg

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Stock Rating Scale	Absolute Return
BUY	>20%
ACCUMULATE	12% to 20%
HOLD	5% to 12%
NEUTRAL	-5% to 5%
REDUCE	-5% to -12%
SELL	<-12%

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