

City Union Bank has reported its Q2 FY22 performance which beat our estimates on almost all front. The bank's profitability was supported by lower provisions, better margin and higher other income.

- **NII came in at INR 4.78 Bn**, 7% QoQ / 1% YoY and 3.5% above our est.
- **Other Income came in at INR 2.03 Bn**, 4% QoQ / 20% YoY and 2% above our est.
- **PPOP came in at INR 4.05 Bn**, 6% QoQ / 5% YoY and 3% above our est.
- **Provisions came in at INR 1.48 Bn**, -13% QoQ / -16% YoY and 5% below our est.
- **PAT came in at INR 1.82 Bn**, 5% QoQ / 15% YoY and 3% above our est.
- **EPS stood at INR 2.46 vs INR 2.34 / INR 2.14** in Q1FY22 / Q2FY21 respectively.

Financial Highlights

- **Asset quality remained stable:** Bank's asset quality stood at the guided path with GNPA/ NNPA of 5.58%/3.48% (down 1 bps QoQ) due to write-offs (Rs 860 Mn vs Rs 2578 Mn QoQ), and recoveries & upgrades (~Rs 1275 Mn vs Rs 822 Mn QoQ). Gross NPA additions amounted to Rs 2974mn for the quarter, translating to an annualized slippage ratio of 3.2% vs 5.4% QoQ.
- Slippages are more front-loaded with higher slippages in H1FY22, implying lower slippages in H2FY22. The bank expects overall slippages for FY22 to be lower than FY21. As the economy gains momentum, we expect normalization of collections and recovery processes to aid asset quality improvement in H2FY22.
- **Advances growth to the pick up pace from Q4FY22:** CUB's advances growth stood 7.3% YoY (up 4.4% QoQ) to Rs 380bn, which was primarily driven by gold loans (+73% YoY/14% QoQ). Management is cautiously optimistic and guides credit growth for FY22E to be in mid to high single-digit. If things stabilize, the bank will press the growth pedal towards the end of FY22.
- On liabilities, the bank is replacing its term deposits with low-cost CASA deposits and maintaining CD ratio at 81-82%, which helped NIMs to stay resilient. Bank's deposit grew by 11.8%YoY/3.8% QoQ led by CASA growth of 26% YoY/9% QoQ taking CASA ratio at 29% (Vs 25.7% YoY/27.6% QoQ).

Financial Summary

Y/E Mar (Rs Bn)	FY20	FY21E	FY22E	FY23E
NII	16.8	18.3	20.8	23.7
Adjusted net profit	4.8	5.9	7.4	9.4
Net worth	53	58	65	74
EPS (Rs)	6	8	10	13
Growth (%)	-30	24	25	27
P/E (x)	25	20	16	13
P/Adj BV (x)	2.7	2.5	2.2	1.9
RoA (%)	1.0	1.2	1.3	1.5
RoE (%)	9.4	10.6	11.9	13.5

Source: Dalal & Broacha Research, Company

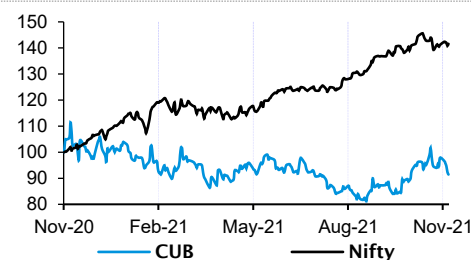
Rating	TP (Rs)	Up/Dn (%)
	202	23

Market data

Current price	Rs	164
Market Cap (Rs.Bn)	(Rs Bn)	121
Market Cap (US\$ Mn)	(US\$ Mn)	1,625
Face Value	Rs	1
52 Weeks High/Low	Rs	200 / 142.55
Average Daily Volume	('000)	1,998
BSE Code		532210
Bloomberg		CUBK.IN

Source: Bloomberg

One Year Performance



Source: Bloomberg

% Shareholding	Sep-21	Jun-21
FII	16.1	17.2
DII	42.1	41.7
Others	41.8	41.2
Total	100	100

Source: BSE

Avinash Tanawade
(022) 67141449
avinash.tanawade@dalal-broacha.com

- As of Sep 30, 2021, CUB's restructured book stood at Rs 22.48 Bn which is 5.9% of gross advances (compared to 5.5% QoQ). ~20% to 25% of the restructures may slip in NPAs over a period of the next two to three years. However, we strongly believe that overall credit loss will be relatively lower as loans are mostly secured. Bank holds a standard account provision on restructured accounts to the tune of Rs.1.67 Bn and Rs.0.46 Bn towards erosion on fair value of accounts.
- Most of the stress came from the services sector (hospitality, tourism, etc.), which has been most impacted due to the lockdowns. SMA-2 stood at 2.8% compared to 3.2% in Q1FY22 and far lower than pre-covid levels of 5-6%.
- The bank has an outstanding of ~Rs19.4 Bn under ECLGS (~5% of total advances). Overall ECLGS started tapering off with 800 borrowers closed their ECLGS accounts over a period of time. ECLGS are given only to those accounts which had satisfactory cash flow and proper track record during pre-COVID days and had temporary cash flow mismatches because of the COVID lockdowns.
- NIMs remained steady:** Bank's NIM stood at 4.03% (vs 3.86% QoQ/4.12% YoY), with Yield on Advances stood at 9.49% (vs 9.40% QoQ/10.21% YoY) and cost of deposits stood at 4.82% (vs 4.95% QoQ/5.54% YoY). We believe that the further decline in the cost of deposits would be limited. Yields compressed as large part of loan growth came from the gold loan segment where the average yield is 8%-9%. The Bank's NIM is expected to remain in the 3.8%-4.2% range for the foreseeable quarters, guided by the management.
- Adequate capital buffer:** Bank's CAR stood at 19.2 % (vs 17.4% YoY/ 19.6% QoQ), of which Tier I capital was 18.2% (vs 16.3% YoY/ 18.5% QoQ). We believe the bank has an adequate capital base and will not be looking at raising capital in the next 12 months.
- Operational efficiency remained healthy:** The bank's operational efficiency remained strong, with cost to income ratio stood at 40.5% (vs 40.3% YoY). The improvement in other income, including the collection from the technically written-off accounts, resulted in maintaining the ratio at ~ 40% against the bank's general guidance of 42% to 45%. The new accounting guidelines will impact the cost to income ratio, as the income from the recovery of technically written-off assets will go to the provisions instead of other income, though it will have a neutral effect on the overall ROA.

CUB's restructured book stood at Rs 22.48 Bn which is 5.9% of gross advances (compared to 5.5% QoQ).

SMA-2 stood at 2.8% compared to 3.2% in Q1FY22 and far lower than pre-covid levels of 5-6%.

The bank has an outstanding of ~Rs19.4 Bn under ECLGS (~5% of total advances).

The Bank's NIM is expected to remain in the 3.8%-4.2% range for the foreseeable quarters, guided by the management.

Bank's CAR stood at 19.2 % (vs 17.4% YoY/ 19.6% QoQ), of which Tier I capital was 18.2% (vs 16.3% YoY/ 18.5% QoQ)

The bank's operational efficiency remained strong, with cost to income ratio stood at 40.5% (vs 40.3% YoY)

Valuation and outlook

CUB's Q2FY22 performance was better than our estimates. While the bank's asset quality will remain elevated in near term, the overall credit loss will be relatively lower, given its proven track record in credit underwriting and unsecured loans of less than 1%. The bank has all the right ingredients, which include conservative management, granular deposit franchise, unparalleled lending franchise, stable margins, and a well-capitalized balance sheet to support future growth. We expect the bank's RoA/RoE to be around 1.3%/11.9% in FY22 and recover back to 1.5%/13.5% in FY23. At the current price, the stock trades at 1.9 times its one-year forward book value, lower than its two-year historical average of 2.4 times and peak valuation of 3.8 times book value. We assign BUY rating with a Target Price of Rs 202/share, valuing the stock at a target multiple of 2.3x FY22E ABV

Financials

Financials (Rs Bn)	Q2FY21	Q3FY21	Q4FY21	Q1FY22	Q2FY22	YoY	QoQ
Interest Earned	10.61	10.48	9.76	9.97	10.22	-4%	2%
Interest Expended	5.86	5.59	5.48	5.50	5.44	-7%	-1%
NII	4.75	4.89	4.29	4.48	4.78	1%	7%
Other Income	1.69	2.30	1.45	1.96	2.03	20%	4%
Net Income	6.44	7.19	5.74	6.43	6.81	6%	6%
Opex	2.60	2.60	2.89	2.60	2.76	6%	6%
PPOP	3.85	4.58	2.85	3.83	4.05	5%	6%
Provisions	1.77	2.19	2.39	1.70	1.48	-16%	-13%
PBT	2.08	2.40	0.46	2.13	2.57	24%	21%
Tax	0.50	0.70	-0.65	0.40	0.75	50%	88%
PAT	1.58	1.70	1.11	1.73	1.82	15%	5%
Balance Sheet							
Deposits	4142	4329	4454	4461	4632	11.8%	3.8%
Advances	3544	3650	3702	3640	3801	7.3%	4.4%
Networth	5571	5741	5842	5998	6169	10.7%	2.9%
Ratios (%)							
GNPA	3.4	2.9	5.1	5.6	5.6	214 bps	-1 bps
NNPA	1.8	1.5	3.0	3.5	3.5	167 bps	-1 bps
PCR	48.3	50.8	43.2	39.0	38.9	-933 bps	-3 bps
Tier 1	16.3	16.3	18.5	18.5	18.2	189 bps	-33 bps
CAR	17.4	17.4	19.5	19.6	19.2	188 bps	-34 bps
Cost/Income	40.3	36.2	50.4	40.5	40.5	20 bps	6 bps
CD Ratio	85.6	84.3	83.1	81.6	82.1	-348 bps	48 bps
Loan Book Sectoral Deployment (%)							
Agriculture	11.3	11.3	13.0	13.7	15.7	443 bps	201 bps
MSME	34.7	34.9	39.6	38.0	37.3	260 bps	-74 bps
Large Industries	5.8	5.1	1.8	1.8	1.6	-415 bps	-11 bps
Retail Traders	1.8	1.5	1.6	2.1	2.7	88 bps	66 bps
Wholesale Traders	13.0	12.6	12.6	12.3	11.9	-110 bps	-40 bps
Commercial Real Estate	7.7	7.2	6.9	6.4	6.2	-144 bps	-14 bps
JL NonAgriculture	6.2	8.2	9.3	9.9	8.8	260 bps	-107 bps
Housing Loans	6.3	6.0	5.7	5.6	5.3	-101 bps	-29 bps
Other Personal Loans	2.7	2.4	2.2	2.6	2.4	-27 bps	-24 bps
Loans backed by Dep	1.4	1.3	1.4	1.4	1.5	8 bps	13 bps
Infrastructure	1.0	0.9	0.8	0.9	0.8	-18 bps	-4 bps
NBFC	0.9	0.8	0.7	0.7	0.9	5 bps	25 bps
Other (EL, Staff Loan, etc)	7.2	7.8	4.4	4.7	4.7	-249 bps	-1 bps

Source: Dalal & Broacha Research, Company

Financial

P&L (Rs Bn)	FY20	FY21	FY22	FY23
Interest income	41.7	41.3	45.1	51.7
Interest expense	24.9	23.1	24.3	28.0
NII	16.8	18.3	20.8	23.7
Non-interest income	6.8	7.0	8.0	9.2
Net revenues	23.6	25.3	28.9	32.9
Operating expenses	10.1	10.5	11.7	13.2
PPOP	13.4	14.8	17.2	19.7
Provisions	7.6	7.9	7.3	7.1
PBT	5.9	6.9	9.9	12.6
Tax	1.1	1.0	2.5	3.2
PAT	4.8	5.9	7.4	9.4
Balance sheet				
Balance sheet	FY20	FY21	FY22	FY23
Share capital	0.7	0.7	0.7	0.7
Reserves & surplus	52	58	65	73
Net worth	53	58	65	74
Deposits	408	445	494	565
Borrowings	20	13	12	12
Other liability	16	16	17	18
Total liabilities	497	533	588	669
Fixed assets				
Fixed assets	2	2	2	3
Investments	91	94	108	119
Loans	339	362	395	454
Cash	47	56	63	72
Other assets	17	19	19	21
Total assets	497	533	588	669

Ratios	FY20	FY21	FY22	FY23
Growth (%)				
NII	4.0	9.2	13.8	13.9
PPOP	8.2	10.6	15.9	14.5
PAT	-30.2	24.5	24.5	27.3
Advances	3.8	6.6	9.2	14.9
Deposits	6.2	9.1	10.9	14.4
Spread (%)				
Yield on Funds	9.2	8.4	8.4	8.5
Cost of Funds	6.1	5.2	5.0	5.2
Spread	3.1	3.2	3.3	3.4
NIM	3.7	3.7	3.9	3.9
Asset quality (%)				
Gross NPAs	4.1	5.1	4.2	3.4
Net NPAs	2.3	3.0	2.6	2.0
Provisions	45	43	40	42
Return ratios (%)				
RoE	9.4	10.6	11.9	13.5
RoA	1.0	1.2	1.3	1.5
Per share (Rs)				
EPS	6	8	10	13
BV	72	79	88	100
ABV	61	65	75	88
Valuation (x)				
P/E	25.3	20.4	16.4	12.9
P/BV	2.3	2.1	1.9	1.6
P/ABV	2.7	2.5	2.2	1.9

Disclaimer

Dalal & Broacha Stock Broking Pvt Ltd, hereinafter referred to as D&B (CINU67120MH1997PTC111186) was established in 1997 and is an integrated financial services player offering an extensive range of financial solutions and services to a wide spectrum of customers with varied needs ranging from equities to mutual funds to depository services.

D&B is a corporate trading member of Bombay Stock Exchange Limited (BSE), National Stock Exchange of India Limited (NSE). D&B along with its affiliates offers the most comprehensive avenues for investments and is engaged in the securities businesses including stock broking (Institutional and retail), depository participant, portfolio management and services rendered in connection with distribution of primary market issues and financial products like mutual funds, fixed deposits. Details of associates are available on our website i.e. www.dalal-broacha.com

D&B is registered as Research Analyst with SEBI bearing registration Number INH000001246 as per SEBI (Research Analysts) Regulations, 2014.

D&B hereby declares that it has not defaulted with any stock exchange nor its activities were suspended by any stock exchange with whom it is registered in any time in the past. It has not been debarred from doing business by any Stock Exchange / SEBI or any other authorities; nor has its certificate of registration been cancelled by SEBI at any point of time.

SEBI and Stock Exchanges have conducted the routine inspection and based on their observations have issued advice letters or levied minor penalty on D&B for certain operational deviations in routine course of business.

D&B offers research services to clients as well as prospects. The analyst for this report certifies that all of the views expressed in this report accurately reflect his or her personal views about the subject company or companies and its or their securities, and no part of his or her compensation was, is or will be, directly or indirectly related to specific recommendations or views expressed in this report.

Other disclosures by D&B (Research Entity) and its Research Analyst under SEBI (Research Analyst) Regulations, 2014 with reference to the subject company(s) covered in this report:-

D&B or its associates may have financial interest in the subject company.

D&B or its associates do not have any material conflict of interest in the subject company.

The Research Analyst or Research Entity (D&B) has not been engaged in market making activity for the subject company.

D&B or its associates may have actual/beneficial ownership of 1% or more securities of the subject company at the end of the month immediately preceding the date of publication of Research Report.

Disclosures in respect of Research Analyst:

Whether Research Analyst or his/her relatives have actual/beneficial ownership of 1% or more securities of the subject company at the end of the month immediately preceding the date of publication of Research Report:	No
Whether the Research Analyst or his/her relative's financial interest in the subject company.	No
Whether the research Analyst has served as officer, director or employee of the subject company	No
Whether the Research Analyst has received any compensation from the subject company in the past twelve months	No
Whether the Research Analyst has managed or co-managed public offering of securities for the subject company in the past twelve months	No
Whether the Research Analyst has received any compensation for investment banking or merchant banking or brokerage services from the subject company in the past twelve months	No
Whether the Research Analyst has received any compensation for products or services other than investment banking or merchant banking or brokerage services from the subject company in the past twelve months	No
Whether the Research Analyst has received any compensation or other benefits from the subject company or third party in connection with the research report	No

D&B and/or its affiliates may seek investment banking or other business from the company or companies that are the subject of this material. Our salespeople, traders, and other professionals may provide oral or written market commentary or trading strategies to our clients that reflect opinions that are contrary to the opinions expressed herein, and our proprietary trading and investing businesses may make investment decisions that may be inconsistent with the recommendations expressed herein.

In reviewing these materials, you should be aware that any or all of the foregoing, among other things, may give rise to real or potential conflicts of interest including but not limited to those stated herein. Additionally, other important information regarding our relationships with the company or companies that are the subject of this material is provided herein. This report is not directed to, or intended for distribution to or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction where such distribution, publication, availability or use would be contrary to law or regulation or which would subject D&B or its group companies to any registration or licensing requirement within such jurisdiction. Specifically, this document does not constitute an offer to or solicitation to any U.S. person for the purchase or sale of any financial instrument or as an official confirmation of any transaction to any U.S. person. Unless otherwise stated, this message should not be construed as official confirmation of any transaction. No part of this document may be distributed in Canada or used by private customers in United Kingdom. All material presented in this report, unless specifically indicated otherwise, is under copyright to D&B. None of the material, nor its content, nor any

copy of it, may be altered in any way, transmitted to, copied or distributed to any other party, without the prior express written permission of D&B . All trademarks, service marks and logos used in this report are trademarks or registered trademarks of D&B or its Group Companies. The information contained herein is not intended for publication or distribution or circulation in any manner whatsoever and any unauthorized reading, dissemination, distribution or copying of this communication is prohibited unless otherwise expressly authorized. Please ensure that you have read "Risk Disclosure Document for Capital Market and Derivatives Segments" as prescribed by Securities and Exchange Board of India before investing in Indian Securities Market. In so far as this report includes current or historic information, it is believed to be reliable, although its accuracy and completeness cannot be guaranteed.

Name	Designation	Email	Phone	Sector
Mr.Kunal Bhatia	Head of Research	kunal.bhatia@dalal-broacha.com	022 67141442	Retail FMCG Logistics
Mrs.Charulata Gaidhani	Sr.Analyst	charulata.gaidhani@dalal-broacha.com	022 67141446	Pharma Healthcare
Mr.Mayank Babla	Sr.Analyst	mayank.babla@dalal-broacha.com	022 67141412	IT Telecom Media
Mr.Avinash Tanawade	Sr.Analyst	avinash.tanawade@dalal-broacha.com	022 67141449	BFSI
Mr.Akshay Ashok	Sr.Analyst	akshay.ashok@dalal-broacha.com	022 67141486	BFSI
Mr.Bhavya Gandhi	Associate	bhavya.gandhi@dalal-broacha.com	022 67141444	Midcaps
Mr.Miraj Shah	Associate	miraj.shah@dalal-broacha.com	022 67141489	FMCG Retail

Address: - 508, Maker Chambers V, 221 Nariman Point, Mumbai 400 021 .

Tel: 91-22- 2282 2992 | E-mail: e_quity.research@dalal-broacha.com