

SMALL STAR SPARKLING BRIGHT!

9th March, 2016

CMP: Rs. 89
Target Price: Rs. 116
Recommendation: BUY

Stock Info

BSE Group	A
BSE Code	532210
NSE Symbol	CUB
Bloomberg	CUBK.IN
Reuters	CUBK.BO
BSE Sensex	24,793
NSE Nifty	7,531

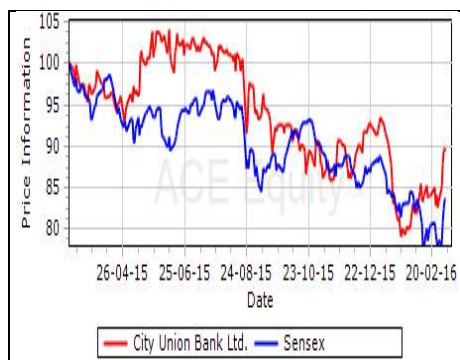
Market Info

Market Capital(Rs Cr)	5,311
Equity Capital(Rs Cr)	59.8
Avg. Trading Vol.	6,92,950
52 Wk High/ Low	106/77
Face Value	1

Shareholding Pattern (%) (Dec 2015)

Promoters	0.0
Domestic Institutions	9.8
Foreign Institutions	37.5
Public & Others	52.7

Price Chart:



Background:

City Union Bank Ltd, the oldest private sector bank in India, was founded on October 31, 1904 and is headquartered at Kumbakonam, Tamil Nadu, India. The bank in the beginning preferred the role of a regional bank. The first branch of the Bank was opened at Mannargudi on 24th January 1930. Presently the bank has pan India presence & operates through 500 branches, 1302 ATM & employee strength of 4,437. The bank has greater presence in Tamil Nadu (about 70%). The main focus of the Bank is lending to MSME, Retail / Wholesale Trade with granular asset profile including providing short term and long term loans to agricultural sector.

Investment Argument:

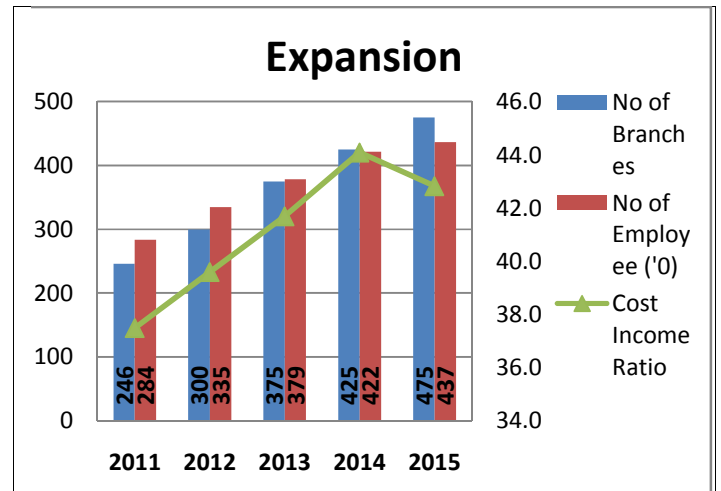
- The bank has diversified loan book with greater exposure to the MSME sector. The small-ticket loans along with the shrinking financial health of the PSU banks are likely to lead the road ahead for the bank. We expect the bank to grow at a CAGR of 16% for FY15-17E.
- The bank stays strong on capital adequacy. The total capital ratio (Basel II) for the bank in FY 13 stood at 13.98 & grew to 16.59 in FY 15. CAR as per Basel III rose from 15.01 in FY 14 to 16.52 in FY 15. We expect the bank to stay strong on its capital adequacy for FY15-17E with a slight drop in FY16.
- The bank manages the costs efficiently. In FY 15 the cost to income ratio dropped down to 42.8 from 44.1 in FY 14. This year (9M) too, the ratio has dropped down to 40.23. This is likely due to the decelerating growth in branches & employee strength.
- The bank continues to keep its NIM healthy. Net interest income for the bank has been on a consistent rise with NIM above 3% for nearly a decade.

SNAPSHOT					
(RS. Cr)	2013	2014	2015	2016E	2017E
Net Interest Income	624	759	807	984	1143
Operating Income	898	1039	1211	1415	1627
Profit After Tax	322	347	395	495	603
ROE	22.3	18.9	16.7	16.8	17.2
P / EPS (x)	7.7	8.4	14.6	10.7	8.9
P / ABV (x)	1.6	1.6	2.3	1.8	1.5

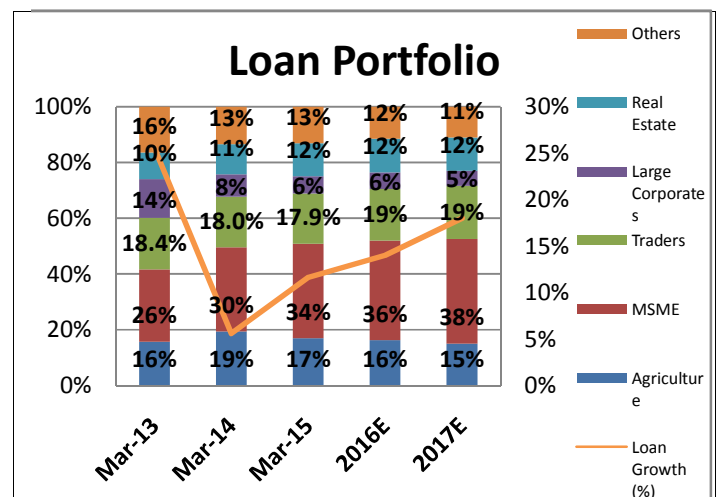
Source: - Company Data Ace Equity, Arianth Research



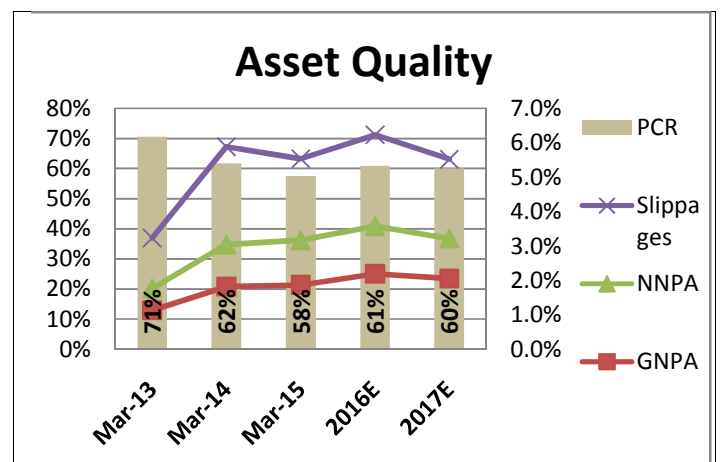
The bank has improved its presence robustly over the years. The period FY 11-13 was led by aggressive growth. The bank's branches grew from 246 in FY 11 to 375 FY 13. Number of employees in the same period grew at CAGR of 15.5%. This however led to the cost income ratio rising from 37.5 in FY 11 to 41.7 in FY 13 & further to 44.1 in FY 14. The cost income ratio however was managed effectively in FY 15, falling to 42.8. For FY 16 the cost income has further dropped to 40.2 for the 9M period. This is likely due to the decelerated growth. We expect cost income ratio to drop down to 34.2 over FY 15-17E.



The loan growth for the bank grew at a CAGR of 18% for FY11-15. This was mainly led by the improving share of MSME which grew from 26% in FY 13 to 34% in FY 15. The share of corporate loans dropped down from 14% in FY 13 to 6% in FY 15. The loans given by the bank are largely small-ticket loans backed by adequate collateral. The diversified loan portfolio reduces credit risk. We peg a CAGR of 16% for FY 15-17E with improving share from traders & MSME segments.

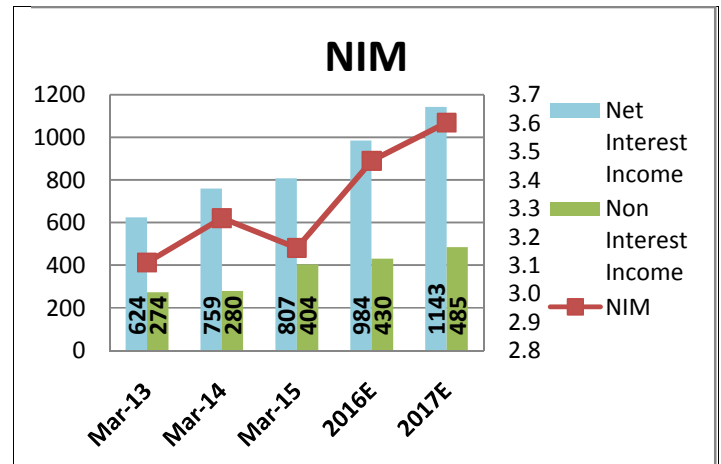


For the period FY 13-15, gross NPA's for the bank doubled from Rs 173 cr to Rs 335 cr. GNPA as a % of advances came in at 1.86 in FY 15 from 1.13 in FY 13. This was due to the rising fresh slippages which rose from 1.5 in FY 13 to 2.4 in FY 15. This was followed by lower provisioning leading to rising net NPA levels. The PCR for FY 15 stood at 58 against 71 in FY 13. Net NPA's rose from 0.63% in FY 13 to 1.3% FY15. PCR however has improved over the 9M of FY 16 to 61% & the GNPA & NNPA as on December quarter stood at 2.4% & 1.5% respectively. We expect slippages to reduce to 2.3% over FY 15-17E & net NPA to drop down to 1.2%.

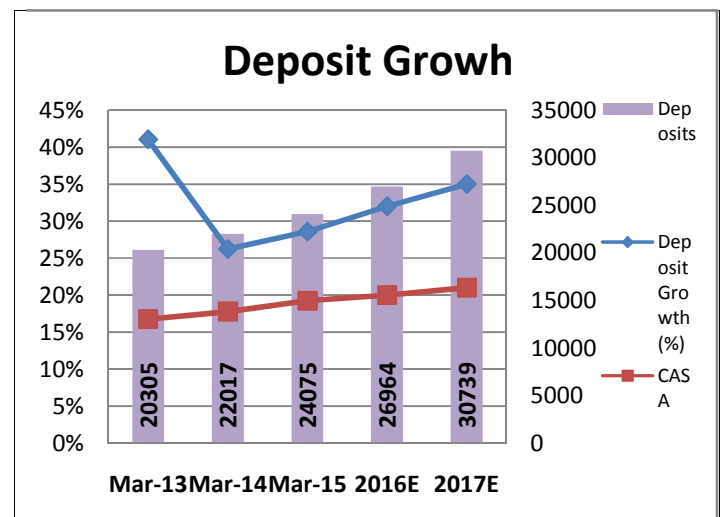




The NIM for the bank has remained healthy. The NIM has been above 3 over the years. For the period FY 13-15 the NIM for the bank grew from 3.11 to 3.16 with a sharp rise in FY 14 to 3.27. We expect NIM to rise further to 3.6 over FY 15-17E. Net interest income for the bank also has grown consistently along with strong support from the non-interest income. For the period FY 13-15 the net interest income grew at a CAGR of 13.7%. We expect the growth in net interest income to further improve going ahead & peg at a CAGR of 19% for FY 15-17E.

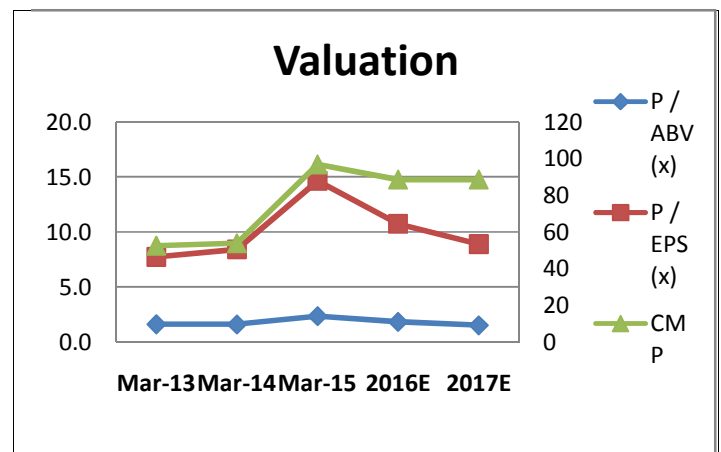


There was a sharp fall in deposit growth in FY 14. The deposits in this year grew at 8.4% falling from 24.3% in FY 13. In FY 15 the deposit grew at 9.3% & we expect it to grow further at a CAGR of 14% for FY 15-17E. CASA portion for the bank has been heading north over the years. From 16.8 in FY 13 it grew to 19.2 in FY 15. We expect it to further grow to 21 in FY 17E. The improving presence of the bank across the nation supports the view to the growth in deposits.



Valuation:

We have valued the bank at its P / ABV multiple of 2.0 (x) to its FY 17E adjusted book value per share. We have arrived at a target of 116 per share at which the valuations look reasonable. At CMP of 89 the stock is trading at the FY 17E P/EPS & P/ABV of 8.9 & 1.5 respectively. We have **“BUY”** rating on the stock.





Income Statement					
(Rs Cr)	2013	2014	2015	2016E	2017E
Interest Earned	2189	2546	2699	3038	3571
Interest Expended	1565	1787	1891	2054	2428
Net Interest Income	624	759	807	984	1143
Other Income	274	280	404	430	485
Fee Income	41	40	43	46	50
Treasury Income	17	23	60	70	85
Operating Income	898	1039	1211	1415	1627
Operating Expenses	374	458	519	542	557
Employee Expenses	151	186	210	218	225
Profit before provision & tax	523	581	693	873	1070
Provisions and Contingencies	120	167	183	215	269
Profit Before Tax	403	414	510	658	801
Provision for tax	81	67	126	162	198
Exp. Items	0	0	11	0	0
Profit After Tax	322	347	395	495	603

Ratios %					
	2013	2014	2015	2016E	2017E
Asset Quality					
Gross NPA	1.1	1.8	1.9	2.2	2.1
Net NPA	0.6	1.2	1.3	1.4	1.2
PCR	70.6	61.7	57.5	61.0	60.0
Growth					
Advances Growth	25.6	5.6	11.6	14.0	18.0
Deposit growth	24.3	8.4	9.3	12.0	14.0
Net Profit Growth	14.9	7.8	13.8	25.3	21.8
Liquidity					
C-D Ratio	75.1	73.1	74.6	76.0	78.6
CASA	16.8	17.8	19.2	20.0	21.0
Capital Adequacy	14.0	15.1	16.6	15.5	16.0
Efficiency					
Cost Income Ratio	41.7	44.1	42.8	38.3	34.2
Operating Costs to Assets	1.6	1.8	1.9	1.7	1.5

Balance Sheet					
(Rs Cr)	2013	2014	2015	2016E	2017E
Sources of funds					
Share Capital	47	54	60	60	61
Total Reserves	1593	1971	2636	3138	3741
Shareholder's Fund	1641	2025	2696	3198	3802
Deposits	20305	22017	24075	26964	30739
Borrowings	477	305	169	135	122
Other Liabilities & provisions	555	647	932	1118	1342
Total Liabilities	22977	24994	27871	31415	36004
Application of Funds					
Cash & Bank	1770	2180	2537	2123	1546
Investments	5267	5954	6365	7320	7832
Advances	15246	16097	17966	20481	24167
Fixed Assets	141	183	210	222	238
Other Assets	552	581	793	1269	2221
Total Assets	22977	24994	27871	31415	36004

	2013	2014	2015	2016E	2017E
Spread Analysis					
Yield on Advances	13.2	13.3	12.7	12.7	13.0
Yield on Investments	7.6	7.8	8.4	8.5	8.6
Cost of Funds	8.4	8.3	8.1	8.0	8.4
Cost of Deposits	8.2	8.2	8.0	8.5	8.4
NIM	3.1	3.3	3.2	3.5	3.6
Interest Spread	4.9	5.1	4.6	4.7	4.6
Profitability					
ROE	22.3	18.9	16.7	16.8	17.2
Earnings Per Share (Rs)	6.8	6.4	6.6	8.3	10.0
Dividend Per Share (Rs)	1.0	1.0	1.1	1.5	2.0
Adjusted Book Value (Rs)	32.5	33.7	41.3	48.6	58.1
Valuation					
P / EPS (x)	7.7	8.4	14.6	10.7	8.9
P / ABV (x)	1.6	1.6	2.3	1.8	1.5

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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%

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