

Industry Financial
Bloomberg CUBK IN
BSE CODE 532210

Steady Performance but NIM remained a concern

RATING **NEUTRAL**

CMP **169**
Price Target **159**
Potential Upside **-6%**

Rating Change 

Estimate Change 

Target Change 

Stock Info

52wk Range H/L 207/134
Mkt Capital (Rs Cr) 12,380
Free float (%) 100%
Avg. Vol 1M (000) 877
No. of Shares (Cr) 73
Promoters Pledged % 0%

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Key Highlights -

- ❑ Focusing on small ticket secured MSME lending; CUB has been growing at an avg. run rate of 17-18% since last few quarters. 52% of the loan book constitutes trading and MSME segments carrying high yields. With the normalization of GST, we expect CUB to grow at 17% CAGR over FY20.
- ❑ Healthy loan growth, strong NIM and controlled assets quality has helped CUB to maintain RoE/ RoA of 15%/1.6% range which is the best among regional bank.
- ❑ Despite the concern over GST impact on assets quality, CUB has been able to control the slippages at sub 2% level. Assets quality has shown improvement but there might be some blip in near term.
- ❑ Due to rising interest rate and limited scope of improvement in yield, NIM is expected to come under pressure. Further with increasing bond yield, treasury gain is also expected to be lower hence the net income growth will moderate in near term.

2Q FY19 Results

CUB's 2Q FY19 numbers were in line with our expectation. NII grew at 12% YoY due to lower NIM which declined by 14 bps YoY but improved by 8 bps sequentially. Other income declined by 24% YoY, due to lower treasury income. Operating profit declined by 8% YoY, mainly due to lower other income and higher opex. Operating expenses grew by 16% YoY, led C/I ratio to jump from 37.3% a year back to 42.7%. Provisions have shown a sharp dip of 47% YoY to Rs 68 Cr. PAT registered 16% YoY growth. GNPA/NNPA improved by 17/1 bps QoQ. PCR declined to 62% as against 65% a quarter back. Loan book grew by 18% YoY.

View and Valuation

Assets quality has seen improvement despite the concern over MSME due to GST transitions reflecting healthy credit underwriting practice. There might be one or two accounts facing funding challenges can slip into NPA in near term which would spike the delinquency ratio but overall management is hopeful to maintain slippages guidance of 1.75-2% in FY19. However due to rising interest rate scenario, we expect NIM to come under pressure as cost will rise going ahead. C/I ratio is expected to increase due to lower income growth than the opex growth. Loan book is expected to grow at steady rate of 18-20% going ahead but deposits growth would be lower due to tightening liquidity scenario. We largely maintain our PAT estimates. We maintain our NEUTRAL stance on the stock due to expected NIM compression and muted operating profit growth. We value it at 2.1x P/BVS FY20e and arrive at a target price of Rs 159.

Key Risks to our rating and target

- ❑ Management's ability to pass on the cost to protect NIM
- ❑ Significant deterioration in assets quality will impact earnings.

KEY FINANCIAL/VALUATIONS	FY16	FY17	FY18	FY19E	FY20E
NII	981	1199	1430	1629	1972
PPP	833	994	1208	1266	1559
PAT	445	503	592	685	847
NIM %	3.5	3.8	4.0	4.0	4.1
EPS (Rs)	6	7	8	9	12
EPS growth (%)	13	13	17	15	24
ROE (%)	15.5	15.2	15.3	15.3	16.3
ROA (%)	1.5	1.5	1.6	1.6	1.7
BV	42	49	57	66	77
P/B (X)	1.9	2.5	2.7	2.6	2.2
P/E (x)	12.7	17.9	19.2	18.1	14.6

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2Q FY19 Results
In-line with expectation
Stable Assets Quality

Financials	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	YoY %	QoQ%	FY17	FY18	YoY %
Interest Inc.	841	865	871	890	926	10.2%	4.2%	3,174	3,402	7.2%
Interest Exp.	486	500	503	515	528	8.7%	2.7%	1,975	1,972	-0.1%
NII	355	365	368	375	398	12.2%	6.2%	1,199	1,430	19.3%
Other Income	155	122	120	129	119	-23.6%	-8.2%	484	532	10.0%
Total Income	510	487	488	504	517	1.3%	2.5%	1,683	1,962	16.6%
Ope Exp.	190	190	193	204	221	16.1%	7.9%	689	755	9.5%
PPP	320	296	294	299	296	-7.5%	-1.2%	994	1,208	21.5%
Provisions	129	86	86	78	68	-47.4%	-12.6%	301	418	38.8%
PBT	191	211	208	222	228	19.5%	2.9%	693	790	14.0%
Tax	46	56	56	60	60	30%	0.0%	190	198	4%
Net Profit	145	155	152	162	168	16.0%	3.9%	503	592	18%

NIM is expected to come under pressure

NIM improved by 8 bps sequentially due to decline in cost of fund, but declined by 14 bps YoY. Yield on advances remained stable QoQ, but declined by 67 bps YoY. Yield on funds declined by 6 bps/25 bps on QoQ/YoY basis. Cost of deposits declined by 8 bps/19 bps on QoQ/YoY mainly due to re-pricing of higher cost deposits at lower rates. Cost of fund declined by 11 bps/21 bps on QoQ/YoY. With the rising interest rate scenario and inability of management to pass on the cost burden will contract the NIM going forward.

C/I ratio jumped by 545 bps to 42.7% YoY, due to increase in the operating expenses by 16% YoY and muted growth in total net income by only 1% YoY. Employee expenses grew by 12% YoY and other operating expenses grew by 19% YoY. Due to lesser treasury gain management expects C/I ratio to remain elevated till the end of FY19. Overall in long term horizon management expect C/I ratio to be in the range of 42-45%.

Advances growth at healthy level but deposits remained moderated.

Advances grew by 18% YoY led by 22% growth in retail and 18% growth in MSME segment. Corporate advances growth moderated to 11% YoY. Loan to Retail traders/Agriculture grew at 22%/17% on YoY basis. NBFC loan growth moderated at 6% YoY as against 28% a quarter back. MSME book share was stable at 34% and traders book share is at 17%. Large industry book share continues to decline at 6.5% vs 7.3% in FY17. Other personal loan share continues to inch up at 4.4% against 3% in FY17. This segment grew by 61% YoY.

Deposits growth picked up to 12% YoY, which is highest in last 6 quarters but the growth remained moderated in comparison to advances growth and hence stretching CD ratio to 85% against 81% a year back. CASA grew at 15% YoY, saving account grew robust by 19% YoY, which is highest in last 5 quarters. Current deposits grew by 9% YoY.

Stable assets quality

Slippage during the quarter has increased by 8% QoQ to Rs 136 Cr. The bank has maintained its asset quality well over a long time by giving small ticket secured loans. The GNPA ratio has declined by 17 bps at 2.85%, whereas NNPA ratio declined marginally by 1 bps at 1.69%.

Standard restructured book stood at Rs 7 Cr. The amount outstanding in security receipts (SR) stood at Rs 331 Cr and total provisioning done towards it is Rs 151 Cr, out of which Rs 16 Cr has been done in 1H FY19. Technical write-off during the quarter stood at Rs 72 Cr. Provision coverage ratio declined to 62% as against 65% a quarter back.

Other highlights:

CAR ratio stood at 15.1% as against 16.1% a quarter back. Tier I ratio stood at 14.7%.

Other income declined by 24% YoY to Rs 119 Cr, led by the decline in treasury income by 67% YoY.

Concall Highlights

- ❑ NIM improved sequentially by 8 bps despite management's expectation of contraction.
- ❑ Due to lesser treasury gain management expects C/I ratio to remain elevated till the end of FY19. Overall in long term horizon management expect C/I ratio to be in the range of 42-45%.
- ❑ Management maintained its credit growth guidance of 18-20% going ahead.
- ❑ Cost of deposits declined as some higher rate deposits raised 3-4 years back got re-priced at lower rates and management don't expect cost of fund to decline further.
- ❑ Provisions breakup- For NPA Rs 47 Cr, Std loan- Rs 2.7 Cr, SR depreciation- Rs 8 Cr and Rs 11 Cr for others.
- ❑ Slippages were disbursed across the sector. About 2-3 accounts together were in the range of Rs 25 Cr from steel and oil sector.
- ❑ In the earlier concall management disclosed the 2 stress accounts one was paper mill and other was educational institute. During the quarter the educational borrower (exposure of Rs 65 Cr) sold some of its property and repaid to the bank. The paper mill (exposure of Rs 85 Cr) has started operation but depends on PSU banks for working capital. If working capital sanctioned by PSU banks then the unit will survive or it will slip to NPA. If it slips then NPA slippages will spike. But management hopes everything to be fine and maintained its earlier slippages guidance of 1.75-2% for FY19.
- ❑ In the paper mill management said that the need of working capital would be around Rs 45 Cr but CUB will not fund it as the coverage to collateral will decline. Management thinks that if this account falls into NPA then they will be able to recover it within 3-4 quarters.
- ❑ Has made provisions of Rs 8 Cr on SRs in line with increasing coverage ratio. Total PCR is 45% on SR. Management will slowly and gradually increase it to 60-65% range by increasing provisions or by way of recovery.
- ❑ CUB has no direct exposure to IL&FS.
- ❑ Has made full provisions on the cyber crime happened last year.
- ❑ There was no sale of any account to ARC and no accounts were restructured during the quarter.

Profitability Matrix

	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	YoY (+/-)	QoQ (+/-)
C/I Ratio %	43.3	37.8	37.3	39.1	39.7	40.6	42.7	5.45	2.13
Empl. Cost/ Tot. Exp. %	41.2	42.3	43.5	42.0	39.7	42.7	42.2	-1.37	-0.54
Other Exp/Tot. Exp.%	58.8	57.7	56.5	58.0	60.3	57.3	57.8	1.37	0.54
Provision/PPP %	28.8	39.3	40.4	28.9	29.3	26.0	23.0	-17.44	-3.01
Tax Rate %	26.9	22.2	24.1	26.6	26.9	27.1	26.3	2.20	-0.75
Int Exp./Int Inc. (%)	61.2	58.5	57.8	57.8	57.7	57.9	57.0	-0.76	-0.83
Other Inc./Net Inc. %	28.8	28.3	30.4	25.0	24.6	25.6	22.9	-7.48	-2.67
PAT/ Net Income %	29.5	29.4	28.4	31.8	31.2	32.1	32.5	4.14	0.44
PAT Growth %	14.8	13.6	17.0	22.2	18.0	15.2	16.0	-0.93	0.85
NII Growth %	17.4	22.3	17.8	18.9	18.5	9.5	12.2	-5.65	2.70
Op. Profit	10.5	26.0	35.2	8.4	18.8	0.8	(7.5)	-42.72	-8.35
RoE %	15.0	15.5	15.2	15.7	15.2	15.3	15.2	-0.04	-0.12
RoA %	1.5	1.6	1.6	1.6	1.6	1.6	1.6	0.04	-0.02

Margin Performance

Margin %	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	YoY (+/-)	QoQ (+/-)
Yield on	11.9	11.8	11.5	11.4	11.2	10.9	10.9	-0.67	0.00
Global Yield on	7.2	6.9	7.0	6.9	6.9	6.9	7.0	-0.06	0.04
Yield on Total	9.3	9.4	9.2	9.2	9.1	9.0	8.9	-0.25	-0.06
Cost of Deposits	6.6	6.4	6.3	6.2	6.2	6.2	6.1	-0.19	-0.08
Cost Of Funds	5.7	5.5	5.3	5.3	5.2	5.2	5.1	-0.21	-0.11
NIM	4.2	4.5	4.5	4.4	4.4	4.2	4.3	-0.14	0.08

Exhibit: Yield and Cost

Both yield and cost of fund declined.

■ Yield on Total Assets % ■ Cost of Deposits %

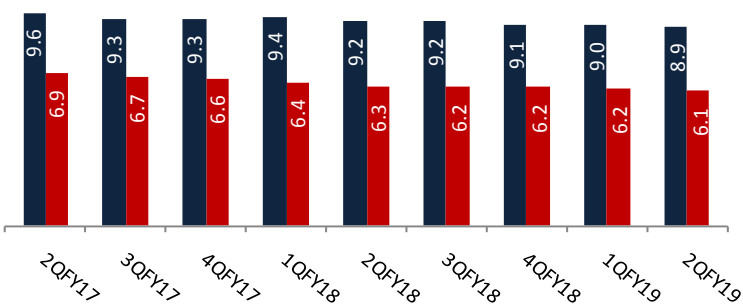
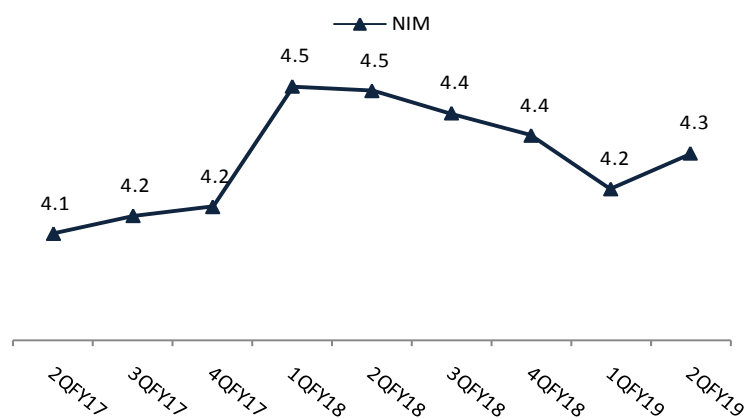


Exhibit: Net Interest Margin

NIM improved.

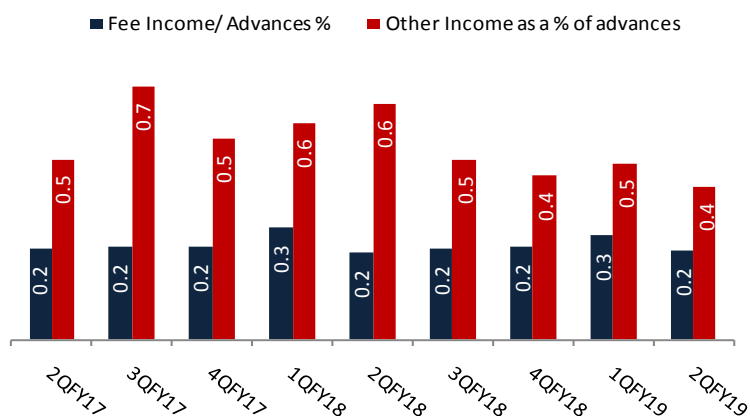


Other Income Break Up-

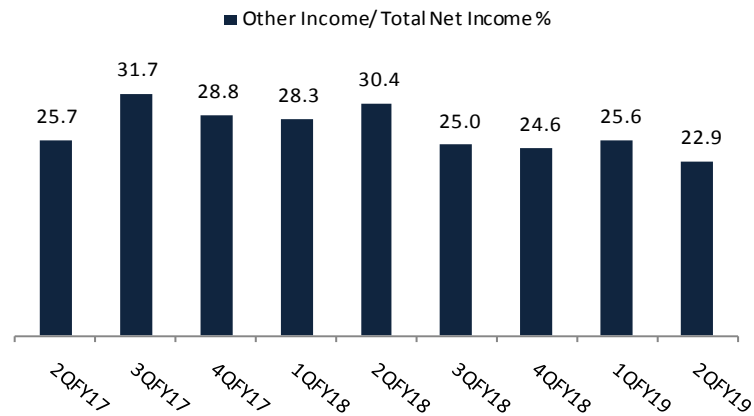
	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19
Commission, Exchange, Bro	52	52	58	70	57	61	68	76	69
Total Fee-Based Income	52	52	58	70	57	61	68	76	69
Growth YoY %	-5	5	8	27	10	17	17	9	20
Treasury Income	42	79	36	39	65	34	30	19	21
Other Inc incl recoveries in v	11	11	32	27	33	26	22	34	28
Other Income	104	143	126	135	155	122	120	129	119
Growth YoY %	10	38	17	22	49	-15	-5	-5	-24

Exhibit: Fee Income/Advances %

Fee income as a % of total advances declined.

**Exhibit: Other Income/ Total Income %**

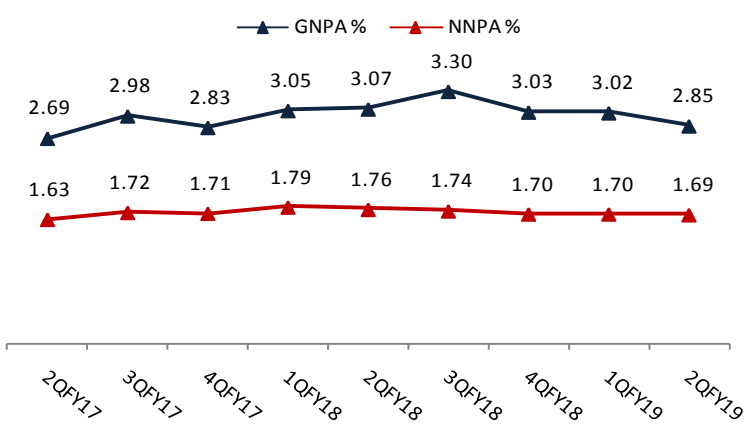
Growth in other income moved down.

**Asset Quality**

	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	YoY (+/-)	QoQ (+/-)
GNPA (Rs in Cr)	682	735	780	860	857	851	848	9%	0%
GNPA %	2.8	3.1	3.1	3.3	3.0	3.0	2.9	-0.22	-0.17
NNPA (Rs in Cr)	408	426	441	448	475	474	498	13%	5%
NNPA %	1.7	1.8	1.8	1.7	1.7	1.7	1.7	-0.07	-0.01
Slippages (Rs in Cr)	139	148	147	132	148	126	136	-7%	8%
PCR %	61.0	62.0	63.0	65.0	64.0	65.0	61.8	-1.20	-3.20

Exhibit: Asset Quality

Assets quality improved.

**Exhibit: Provisions**

PCR declined.

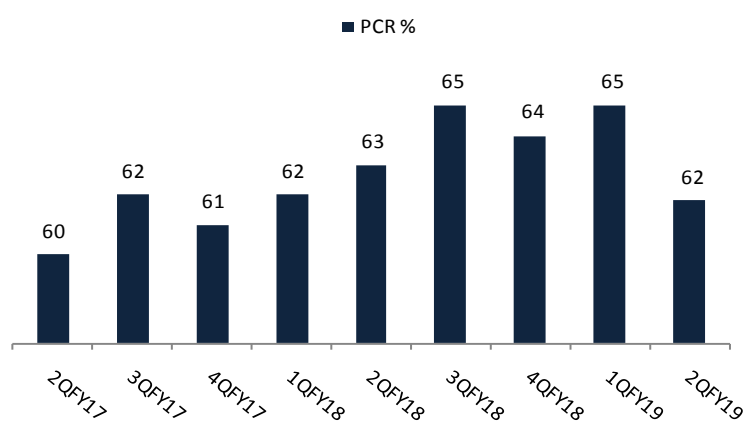
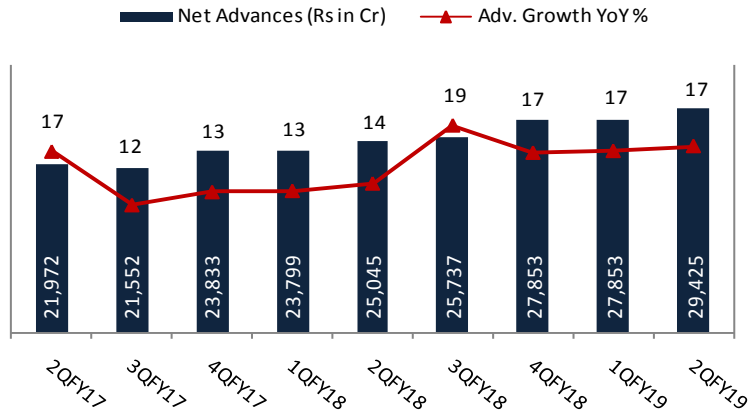
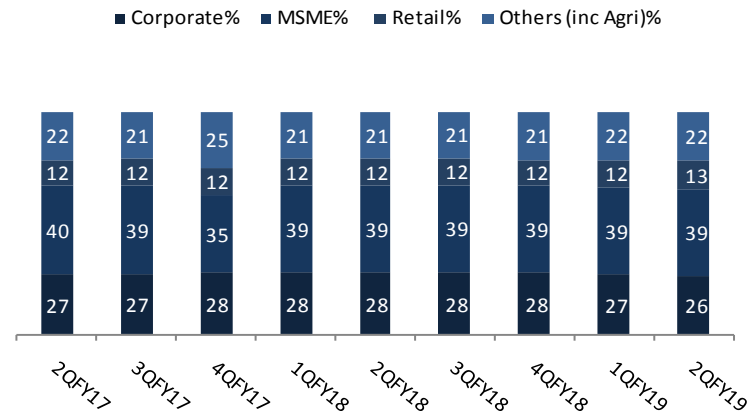
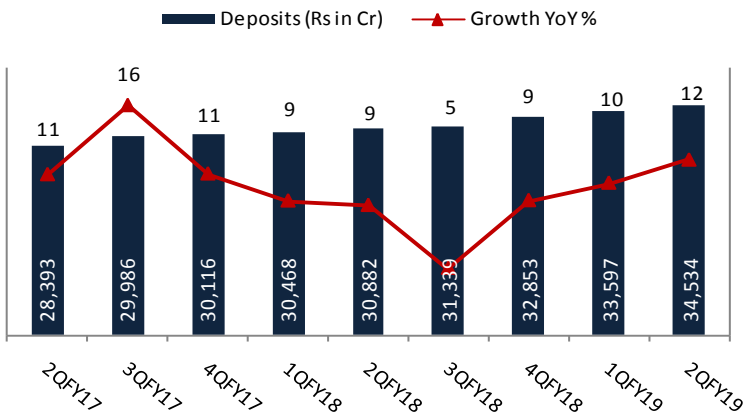
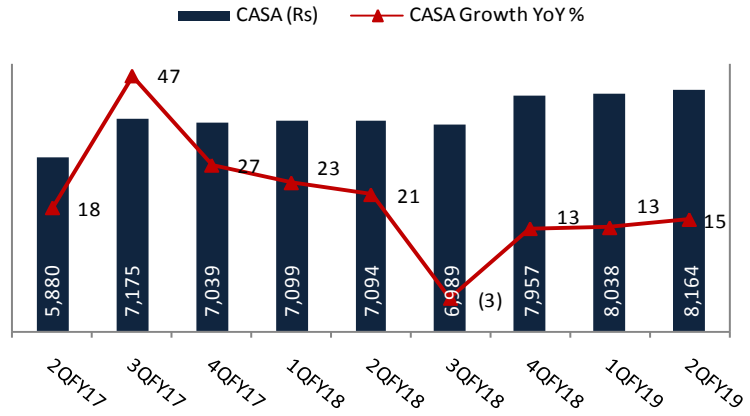
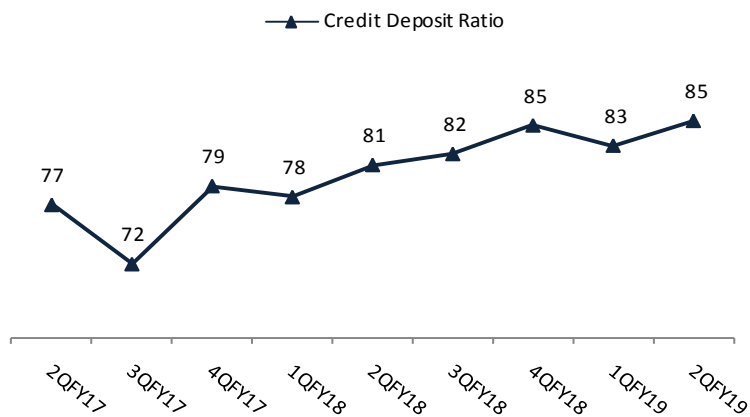
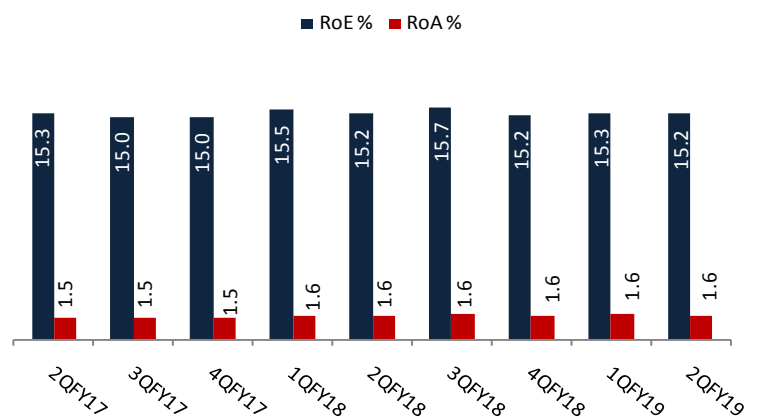


Exhibit: Advances Performance*Advances growth remained muted.***Exhibit: Advances Breakup%***Portfolio has slightly tilted towards retail profile.***Exhibit: Deposits Performance***Deposits growth improved.***Exhibit: CASA Performance***CASA level on improving trend.***Exhibit: Credit Deposit Ratio***CD ratio moved up.***Exhibit: Return Ratios.***Return ratios remained stable.*

Financial Details

Balance Sheet

Y/E March	FY13	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
Share Capital	47	54	60	60	60	66	73	73
>> Equity Capital	47	54	60	60	60	66	73	73
>> Preference Capital	0	0	0	0	0	0	0	0
Reserves & Surplus	1593	1971	2636	2992	3510	4097	4738	5532
Networth	1641	2025	2696	3052	3570	4163	4811	5605
Deposits	20305	22017	24075	27158	30116	32853	37893	44713
Change (%)	24.3	8.4	9.3	12.8	10.9	9.1	15.3	18.0
>> CASA Deposits	3405	3917	4631	5533	7039	7957	9322	11178
Change (%)	14.6	15.1	18.2	19.5	27.2	13.0	17.2	19.9
Borrowings	477	305	169	664	531	1736	1876	1967
Other Liabilities & Prov.	555	647	932	929	1054	1186	1353	1597
Total Liabilities	22977	24994	27871	31804	35271	39937	45933	53883
Cash & Bank	1770	2180	2537	2650	2879	2636	2750	3202
Investments	5267	5954	6365	6826	7031	7879	8940	10549
Change (%)	14.8	13.0	6.9	7.2	3.0	12.1	13.5	18.0
Advances	15246	16097	17966	21057	23833	27853	32588	38454
Change (%)	25.6	5.6	11.6	17.2	13.2	16.9	17.0	18.0
Fixed Assets	141	183	210	218	215	223	230	237
Other Assets	552	581	793	1053	1313	1346	1426	1442
Total Assets	22977	24994	27871	31804	35271	39937	45933	53883

Income Statement

Y/E March	FY13	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
Interest income	2189	2546	2699	2944	3174	3402	3802	4603
Interest expended	1565	1787	1891	1963	1975	1972	2173	2631
Net Interest Income	624	759	807	981	1199	1430	1629	1972
Change (%)	24.9	21.7	6.3	21.5	22.2	19.3	13.9	21.1
Other Income	274	301	404	410	484	532	504	555
Change (%)	32.1	10.1	34.2	1.5	18.0	10.0	-5.2	10.1
>> Core Fee Income	173	174	197	211	218	256	295	326
>> Treasury Income	35	56	129	126	206	168	97	130
>> Others	66	71	78	73	61	108	112	100
Total Net Income	898	1061	1211	1391	1683	1962	2133	2527
Operating Expenses	374	480	519	558	689	755	867	969
Change (%)	33.7	28.2	8.2	7.5	23.5	9.5	14.9	11.7
>> Employee Expenses	151	186	210	213	298	316	358	372
Pre-provisioning Profit	523	581	693	833	994	1208	1266	1559
Change (%)	22.6	11.0	19.2	20.3	19.3	21.5	4.8	23.2
Provisions	120	167	183	231	301	418	329	399
Change (%)	43.7	39.0	9.0	26.3	30.5	38.8	-21.2	21.1
PBT	403	414	521	603	693	790	937	1160
Tax	81	67	126	158	190	198	251	313
Profit After Tax	322	347	395	445	503	592	685	847
Change (%)	14.9	7.8	13.8	12.6	13.1	17.7	15.7	23.6

Financial Details

Key Ratios

Y/E March	FY13	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
Balance Sheet Metrics								
Loan Growth (%)	26	6	12	17	13	17	17	18
Deposit Growth (%)	24	8	9	13	11	9	15	18
C/D Ratio (%)	75.1	73.1	74.6	77.5	79.1	84.8	86.0	86.0
CASA (%)	16.8	17.8	19.2	20.4	23.4	24.2	24.6	25.0
Investment/Deposit (%)	25.9	27.0	26.4	25.1	23.3	24.0	23.6	23.6
CRAR (%)	14.0	15.0	16.5	15.6	15.8	16.2	16.4	16.3
>> Tier 1 (%)	13.3	14.4	16.0	15.1	15.4	15.8	16.0	15.9
>> Tier 2 (%)	0.7	0.6	0.5	0.5	0.5	0.4	0.4	0.4

Assets Quality Metrics

Gross NPA (Rs)	173	293	336	512	682	857	955	1,156
Gross NPA (%)	1.1	1.8	1.9	2.4	2.8	3.0	2.9	3.0
Net NPA(Rs)	96	197	233	323	408	475	544	613
Net NPA (%)	0.6	1.2	1.3	1.5	1.7	1.7	1.7	1.6
Slippages (%)	2	3	4	2	2	2	2	2
Provision Coverage (%)	71	62	58	60	61	64	64	70
Provision/Average Advances (%)	0.9	1.1	1.1	1.2	1.3	1.6	1.1	1.1

Margin Metrics

Yield On Advances (%)	13.2	13.3	12.7	12.1	11.5	11.0	10.5	10.9
Yield On Investment (%)	7.6	7.8	8.4	8.2	7.8	7.0	7.0	7.3
Yield on Earning Assets (%)	11.2	11.3	10.8	10.5	10.0	9.6	9.3	9.7
Cost Of Deposits (%)	8.2	8.2	8.0	7.5	6.8	6.1	6.0	6.1
Cost Of Funds (%)	8.3	8.2	8.0	7.5	6.7	6.0	5.8	6.0
Spread (%)	3.0	3.1	2.8	3.0	3.3	3.6	3.6	3.7
NIM (%)	3.2	3.4	3.2	3.5	3.8	4.0	4.0	4.1

Profitability & Efficiency Metrics

Int. Expense/Int.Income (%)	71.5	70.2	70.1	66.7	62.2	58.0	57.2	57.2
Fee Income/NII (%)	-	-	-	-	18.2	17.9	18.1	16.5
Cost to Income (%)	41.7	45.2	42.8	40.1	40.9	38.5	40.7	38.3
Cost on Average Assets (%)	1.9	2.1	2.1	2.0	2.2	2.1	2.1	2.0
Tax Rate (%)	20.1	16.1	24.2	26.2	27.4	25.1	26.9	27.0

Valuation Ratio Metrics

EPS (Rs)	4.9	5.3	5.5	6.2	7.0	8.2	9.4	11.6
Change (%)	(13.0)	7.0	3.5	12.6	13.1	17	15	23.6
ROAE (%)	22.3	18.9	16.3	15.5	15.2	15.3	15.3	16.3
ROAA (%)	1.6	1.4	1.5	1.5	1.5	1.6	1.6	1.7
Dividend Payout (%)	16.7	15.6	16.6	16.1	3.9	3.7	5.3	5.2
Dividend yield (%)	2.3	2.2	1.4	1.5	0.2	0.2	0.3	0.4
Book Value (Rs)	25.2	30.8	37.3	42.3	49.5	57.3	65.7	76.6
Change (%)	(0)	23	21	13	17	16	15	17
P/B (X)	1.7	1.4	2.1	1.9	2.5	2.7	2.6	2.2
P/E (X)	8.8	8.4	14.6	12.7	17.9	19.2	18.1	14.6

Financial Details

Exhibit: DuPont Analysis

	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
<i>Interest Income</i>	10.6	10.2	9.9	9.5	9.0	8.9	9.2
<i>Interest expended</i>	7.4	7.2	6.6	5.9	5.2	5.1	5.3
<i>Net Interest Income</i>	3.2	3.1	3.3	3.6	3.8	3.8	4.0
<i>Non-Fund Based Income</i>	1.3	1.5	1.4	1.4	1.4	1.2	1.1
>> <i>Core Fee Income</i>	0.7	0.7	0.7	0.6	0.7	0.7	0.7
>> <i>Trading and Other Income</i>	0.5	0.8	0.7	0.8	0.7	0.5	0.5
<i>Core Operating Income</i>	3.9	3.8	4.0	4.2	4.5	4.5	4.6
<i>Total Income</i>	4.4	4.6	4.7	5.0	5.2	5.0	5.1
<i>Total Operating Expenses</i>	2.0	2.0	1.9	2.1	2.0	2.0	1.9
>> <i>Employee Expenses</i>	0.8	0.8	0.7	0.9	0.8	0.8	0.7
>> <i>Other Expenses</i>	1.2	1.2	1.2	1.2	1.2	1.2	1.2
<i>Operating Profit</i>	2.4	2.6	2.8	3.0	3.2	2.9	3.1
<i>Provisions</i>	0.7	0.7	0.8	0.9	1.1	0.8	0.8
<i>Others</i>	-	0.0	-	-	-	-	-
<i>PBT</i>	1.7	1.9	2.0	2.1	2.1	2.2	2.3
<i>Tax</i>	0.3	0.5	0.5	0.6	0.5	0.6	0.6
<i>PAT/RoAA</i>	1.4	1.5	1.5	1.5	1.6	1.6	1.7
<i>Equity Multiplier (x)</i>	13.1	11.2	10.4	10.1	9.7	9.6	9.6
<i>ROAE</i>	18.9	16.3	15.5	15.2	15.3	15.3	16.3

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*The name of the Company has been changed from "Microsec Capital Limited" to "Narnolia Financial Advisors Limited" pursuant to change of control. The change in name has been duly effected in the records of the Registrar of Companies (ROC). The application for fresh registration in the new name of "Narnolia Financial Advisors Limited" pursuant to change of control is under process with SEBI.

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