

Canara Bank (CBK IN)

Operating performance risk remains

INDIA | BANKING | Quarterly Update

30 May 2016

Top takeaways from Q4FY16

- ✗ Performance at the operating level continued to remain weak due to negative credit growth and subdued NIM, this was further accentuated by cleaning up of balance sheet leading to higher NPA provisions and resulting in loss of Rs 39bn.
- ✗ NII declined (-5% yoy) to Rs 23.7bn led by interest reversal on NPAs (Rs 2.8bn) and due to decline in credit (-2% yoy).
- ✗ Asset quality hit bottom as slippages soared to Rs 146bn (Rs 54bn in Q2FY16) due to cleaning up of balance sheet. GNPA/NNPA increased 356bps/252bps qoq to 9.4%/6.4%.
- ✓ Management expects to contain slippage to the extent of upgrade/recovery in FY17.

Key highlights

- Loan-book declined (-2% yoy) due to fall in corporate loans (-19%). However, retail loan book grew 28% driven by strong growth in mortgages (39% yoy). While agri/MSME were up 14%/10%.
- Non-interest income growth was modest at 4% yoy, although higher than our subdued expectation, led by higher treasury gains (Rs 3.4 bn). Core fee income declined 7% yoy to Rs 2.5bn.
- NIMs declined 5bps yoy to 2.19% due to decline in yield on advances on account of interest reversal of Rs 2.8bn. on a sequential basis NIM increased 3 bps due to decline in cost of funds.

Management comments / concall takeaways

- ✗ Of the total slippages of Rs 145 bn (Rs 21 bn from restructured), AQR related slippages was Rs 30bn (total AQR slippages Rs 44.6bn). AQR related provisions Rs 25.7 bn (Rs 6bn in Q4).
- ✓ Rs 80-100bn recovery/upgradation target for Rs FY17. GNPA target of 5% in FY17.
- ✗ Initiated SDR in one account amounting to Rs 11.9bn, outstanding stock of SDR at Rs 49.9bn. Outstanding 5/25 at Rs 60bn (12 accounts).
- ✓ SMA -2 consists of Rs 55bn (1.7% of loan book), there are no critical accounts; in Q3 FY16 SMA- 2 was 120 bn.

Outlook and valuation: Weak operating metrics, coupled with high provisioning requirement will keep earnings subdued in FY17, translating into weak returns ratio, thus overshadowing cheap valuation. Incrementally, equity dilution will be book-value decreative. Due to lack of earnings visibility and erosion in book value we maintain Neutral with a PT of Rs 200 (Rs 320 earlier). At CMP of Rs 193, the stock trades at 1.1x our FY17 ABVPS of Rs 180 and 0.8x our FY18 ABVPS of Rs 237.

Neutral (Maintain)

CMP RS 193/ TARGET RS 200 (+4%)

COMPANY DATA

O/S SHARES (MN) :	543
MARKET CAP (RSBN) :	105
MARKET CAP (USDBN) :	1.6
52 - WK HI/LO (RS) :	360 / 156
LIQUIDITY 3M (USDMN) :	10.
PAR VALUE (RS) :	10

SHARE HOLDING PATTERN, %

	Dec 15	Sep 15	Jun 15
FII / NRI :	66.3	66.3	64.5
FI / MF :	7.5	7.5	8.2
NON PRO :	19.5	19.5	20.7
PUBLIC :	0.8	0.8	0.7
GOVT :	5.9	5.9	6.0

Key Financials

Rs mn	FY16	FY17E	FY18E
Pre-prov ROE (%)	27.2	25.1	26.0
Pre-prov ROA (%)	1.4	1.2	1.3
Net Profit	-28,128	16,140	25,268
% growth	NA	NA	56.6
Adj BVPS (Rs)	151.0	180.2	237.1
ROE (%)	(10.7)	5.9	8.5
P/E (x)	-3.7	6.9	4.6
Adj P/BV (x)	1.28	1.07	0.81
EPS (Rs)	-51.8	28.3	41.5

CHANGE IN ESTIMATES

Rs bn	Revised Est.		% Revision	
	FY17E	FY18E	FY17E	FY18
NII	96.6	110.8	-9.9	-9.5
PPP	68.5	77.0	-3.5	-4.2
Core PAT	16.1	25.3	-33.8	-27.5
EPS (Rs)	27.8	41.5	-42.3	-36.3

Manish Agarwalla, Pradeep Agrawal, Pares Jain

(Rs bn)	Q4FY16	Q4FY15	yoy %	Q3FY16	qoq %	vs. expect. %	Comments
Net interest income	23.7	24.9	-4.5	22.3	6.6	8.5	NII was subdued due to decline in credit growth and fall in NPA
NIM (%)	2.2	2.3	(6bps)	2.2	3bps	8bps	Interest reversal lead to decline in NPA
Advances	3247.1	3300.4	-1.6	3319.1	-2.2	-6.3	Advances declined due to fall in corporate loan book
Corporate advances	1367.8	1682.7	-18.7	1521.7	-10.1		De-risking in corporate segment led to decline
Retail advances	540.7	423.0	27.8	484.5	11.6		Home loan 38% yoy; education loan 20% yoy
Deposit	4797.9	4738.4	1.3	4906.0	-2.2		Term deposits declined 1.1% yoy, CASA deposits grew 9% yoy
CASA	1235.4	1135.3	8.8	1181.3	4.6		Savings and Demand deposit grew 11% and -0.1% respectively
CASA %	27.4	25.5	191bps	25.7	167bps		CASA improvement due to decline in term deposit
Core fee	4.4	3.3	34.2	4.4	0.7	3.0	Fee income remains muted due to lack of pick up in corporate activity
Trading gain	3.4	5.1	-34.0	1.6	108.7		
Operating expenses	21.1	20.8	1.5	18.4	14.5	10.5	Employee expenses grew 7% yoy, other opex declined 5% yoy
Cost to income ratio (%)	61.7	63.0	(128bps)	57.0	471bps		
Provision	63.3	10.1	527.2	14.3	343.1	423.3	NPA Rs 58.9bn; invest. Rs -850mn, std. Rs -2.8bn, rest. & others Rs 4.4bn
PAT	-39.1	6.1	-737.9	0.8	-4696.3	NA	Net loss due to high NPA provision
Slipage	146.0	28.1	420.6	54.0	170.3		AQR related slippages Rs 29.9bn, slippages from restructured loans Rs 21bn
GNPA	9.4	3.9	551bps	5.8	356bps		GNPA soared due to cleaning up of balance sheet
NNPA	6.4	2.7	377bps	3.9	252bps		PCR ratio declined 385 qoq to 50.1%
Tier 1 Capital %	8.8	8.0	78bps	8.7	12bps		CET -1 at 8.18%

Result Update

(Rs mn)	Q4FY16	Q4FY15	YoY growth	Q3FY16	QoQ growth
Interest earned	1,07,329	1,11,027	-3.3	1,08,821	-1.4
Interest expended	83,592	86,173	-3.0	86,555	-3.4
Net interest income	23,738	24,854	-4.5	22,266	6.6
Net interest margins	2.19	2.25	-0.1	2.16	0.0
Non-interest income	13,832	13,258	4.3	11,686	18.4
Total Income	37,570	38,113	-1.4	33,952	10.7
Total operating expenses	21,104	20,794	1.5	18,427	14.5
Payroll costs	12,395	11,625	6.6	10,398	19.2
Others	8,709	9,169	-5.0	8,030	8.5
Pre-provision Profit	16,466	17,318	-4.9	15,524	6.1
Provisions & Contingencies	63,315	10,096	527.2	14,289	343.1
% Operating income	384.5	58.3	326.2	92.0	292.5
PBT	-46,850	7,223	-748.7	1,236	-3,890.8
Provision for Taxes	-7,795	1,100	-808.6	386	-2,118.4
% of PBT	16.6	15.2	1.4	31.2	-14.6
Net Profit	-39,055	6,123	-737.9	850	-4,696.3
Equity	5,430	4,752	14.3	5,430	0.0
EPS, Rs	-71.9	12.9	-658.2	1.6	-4,696.3
Advances	32,47,148	33,00,355	-1.6	33,19,149	-2.2
Deposits	47,97,916	47,38,401	1.3	49,05,989	-2.2
Advances / Deposits (%)	67.7	69.7	-2.0	67.7	0.0
Gross NPAs	3,16,378	1,30,400	142.6	1,98,134	59.7
Gross NPAs (%)	9.4	3.9	5.5	5.8	3.6
Net NPAs	2,08,329	87,401	138.4	1,29,401	61.0
Net NPAs (%)	6.4	2.7	3.8	3.9	2.5
CAR – Total	11.1	10.6	0.5	11.5	-0.5

Source: Company, PhillipCapital India Research

Financials

Income Statement

Y/E Mar, Rs mn	FY15	FY16	FY17e	FY18e
Interest on Loans	3,20,661	3,13,773	3,20,048	3,60,054
Interest on Investments	1,09,238	1,14,078	1,19,782	1,34,755
Others	7,602	12,371	13,608	14,424
Total Interest Earned	4,37,500	4,40,221	4,53,438	5,09,233
Total Interest Expended	3,40,864	3,42,588	3,56,840	3,98,390
Net Interest Income	96,637	97,634	96,597	1,10,843
Total non interest income	45,503	48,752	52,221	55,135
Total Income	1,42,139	1,46,386	1,48,818	1,65,979
Personnel Expenses	42,743	44,459	48,016	53,297
Other Expenses	29,893	30,461	32,256	35,652
Total Op expenses	72,636	74,919	80,271	88,949
Net Inc (Loss) before prov	69,504	71,467	68,547	77,030
Provision and coningencies	34,527	1,03,324	48,372	43,340
Net Inc (Loss) before tax	34,976	-31,858	20,175	33,690
Provision for Income Tax	7,950	-3,730	4,035	8,423
Net Profit	27,026	-28,128	16,140	25,268

Balance Sheet

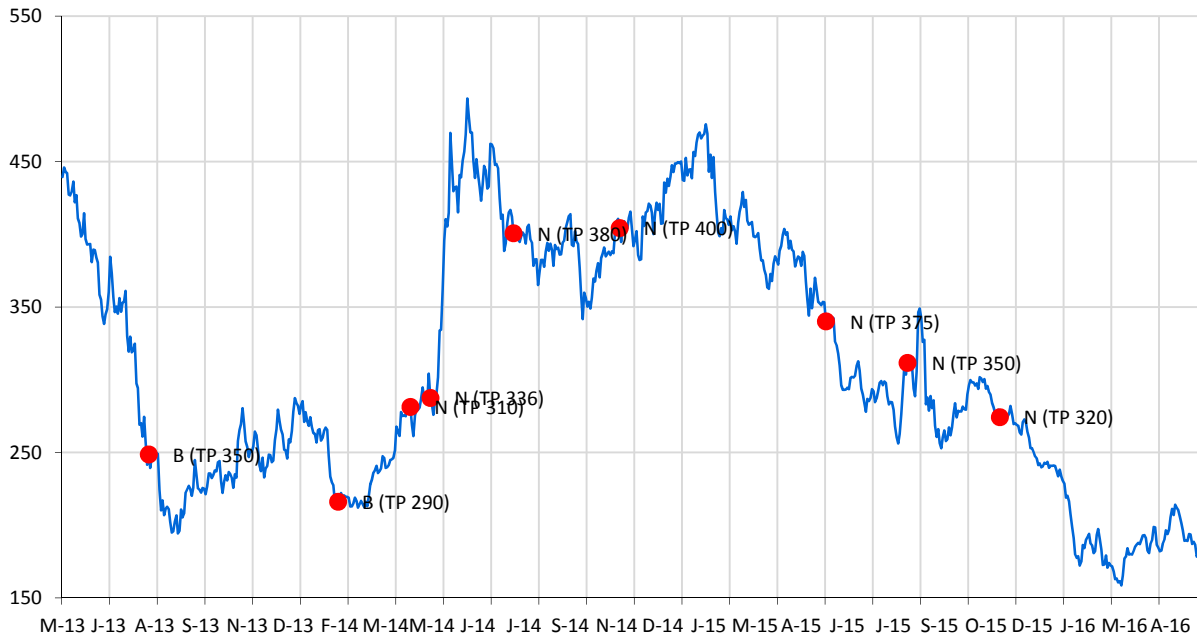
Y/E Mar, Rs mn	FY15	FY16	FY17e	FY18e
Assets				
Cash & Bal with RBI	4,86,411	5,67,337	6,29,744	6,99,015
Loans, Adv & Int accrued	33,00,355	32,47,148	35,06,920	39,78,725
Investments	14,53,462	14,23,093	16,06,152	18,06,012
Fixed Assets (Net)	69,494	71,981	79,179	87,097
Other assets	1,70,283	2,20,049	3,53,134	3,96,372
Total Assets	54,80,006	55,29,608	61,75,129	69,67,222
Liabilities				
Share capital	4,752	5,430	5,809	6,090
Reserves and Surplus	2,59,785	2,56,156	2,77,989	3,01,787
Hybrid Capital	19,187	21,682	24,500	27,685
Debt	90,090	1,00,900	1,14,017	1,28,840
Borrowing	1,47,439	1,46,151	1,68,074	1,93,285
Total Deposits	47,55,517	48,17,598	53,90,325	61,01,123
Other liab incld prov	1,49,181	1,27,244	1,39,969	1,53,965
Total Liabilities	54,80,006	55,29,608	61,75,129	69,67,222

Source: Company, PhillipCapital India Research Estimates

Valuation Ratios

	FY15	FY16	FY17e	FY18e
Earnings and Valuation Ratios				
Pre-provision Operating RoAE (%)	27.5	27.2	25.1	26.0
RoAE (%)	10.7	(10.7)	5.9	8.5
Pre-provision Operating ROA (%)	1.3	1.3	1.2	1.2
RoAB (%)	0.54	-0.54	0.29	0.41
EPS (Rs.)	56.9	(51.8)	27.8	41.5
Dividend per share (Rs.)	11.4	0.0	5.0	7.0
Book Value (Rs.)	670.4	582.0	582.3	594.9
Adj BV (Rs.)	356.8	151.0	180.2	237.1
Revenue Analysis				
Interest income on IBA (%)	8.8	8.4	8.3	8.3
Interest cost on IBL (%)	7.2	6.8	6.6	6.6
NIM on IBA / AWF (%)	1.9	1.9	1.8	1.8
Core fee Inc / AWF (%)	0.3	0.3	0.3	0.3
Portfolio gains / Total Inc (%)	8.8	7.3	6.8	5.1
Op.Exp / TI (%)	55.6	54.9	57.6	56.3
Op.Exp / AWF (%)	1.5	1.4	1.5	1.5
Employee exps / Op exps (%)	58.8	59.3	59.8	59.9
Tax / Pre-tax earnings (%)	22.7	11.7	20.0	25.0
Asset Quality				
GNPAs / Gr Adv (%)	4.0	9.7	9.3	7.7
NNPAs / Net Adv (%)	2.7	6.6	6.1	4.8
Growth Ratio				
Loans (%)	9.6	(1.6)	8.0	13.5
Investments (%)	14.6	(2.1)	12.9	12.4
Deposits (%)	12.6	1.3	11.9	13.2
Networth (%)	7.6	(0.8)	7.0	7.1
Net Int Income (%)	8.0	1.0	(1.1)	14.7
Non-fund based income (%)	3.1	14.2	10.0	10.3
Non-Int Exp (%)	19.4	3.1	7.1	10.8
Profit Before Tax (%)	14.2	(191.1)	(163.3)	67.0
Net profit (%)	10.8	(204.1)	(157.4)	56.6
Asset / Liability Profile				
Avg CASA/ Deposits (%)	24.2	24.8	25.9	26.1
Avg Adv / Avg Dep (%)	68.0	63.7	59.9	59.6
Avg Invst / Avg Dep (%)	30.3	30.0	29.7	29.7
Incr Adv / Deposits (%)	54.3	(85.7)	45.4	66.4
Avg Cash / Avg Dep (%)	10.4	11.0	11.7	11.6
Capital Adequacy Ratio:				
Tier I (%)	10.6	11.1	10.9	10.5
Internal Capital Generation rate (%)	8.0	8.8	8.5	8.2
NNPAs to Equity (%)	9.0	(10.6)	5.1	7.4
	27.4	65.9	61.4	51.1

Stock Price, Price Target and Rating History



Rating Methodology

We rate stock on absolute return basis. Our target price for the stocks has an investment horizon of one year.

Rating	Criteria	Definition
BUY	$\geq +15\%$	Target price is equal to or more than 15% of current market price
NEUTRAL	$-15\% > \text{to} < +15\%$	Target price is less than +15% but more than -15%
SELL	$\leq -15\%$	Target price is less than or equal to -15%.

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