

Canara Bank (CBK IN)

Asset quality pain continues

INDIA | BANKING | Quarterly Update

9 May 2017

Top takeaways from Q4FY17

- ✗ Net profit was below our expectation as the bank created higher due to higher NPA provision resulting in improvement in PCR by 310bps to 55.6%
- ✓ NII was driven (+14% yoy) improved due to marginal pick up in loan growth (+5.3% yoy) and 4bps yoy improvement in NIM to 2.23%.
- ✗ Slippages increased to Rs 31bn (Rs 22.3bn in Q3FY17). However, GNPA declined 34 bps qoq to 9.63% due to higher write offs (Rs 24bn), NNPA declined 39bps qoq to 6.33% due to higher NPA provision and improvement in PCR.
- ✓ Non-interest income included one of gain worth Rs 7bn on sale of stake in Can Fin Homes. While core fee income was buoyant at 45% yoy due to Rs 8.5bn fee earned in sale of PSL securities.
- ✓ Loan-book growth picked up marginally driven by SME (11.4% yoy), Agri, (+10% yoy) and retail (+90% yoy). corporate loans growth continued to remain weak (-1.5% yoy).

Management comments / concall takeaways

- ✓ SMA-2 loans have declined to Rs 80.3bn from Rs 180bn sequentially.
- ✓ NPAs have largely come from
- ✓ portfolio. YTM on investment book is 7.75%
- ✓ Will sell stake in Canbank factors steel, infra and road sector.
- ✓ Will bring down GNPA below 6% by H1FY18.
- ✓ Have not taken any MTM hit on investment in FY18, will not sell further stake in Can-Fin Homes.
- ⇔ Outstanding stock of SDR/S4A/5:25 at Rs 70bn/ 40bn/63bn (all accounts are standard).
- ⇔ Steel NPL at Rs 110bn (NPA 68%). Power sector exposures Rs 222bn (private Rs 150bn, PSU RS 32bn) and NPAs at 7%.
- ⇔ FY18 guidance – Advance growth 11-12%, deposit growth 7-8%, CASA growth- 35%, slippage ratio – 1.5%, F18 credit cost to be lower than FY17.

Outlook and valuation: The recent run up in the stock price is factoring various NPA resolutions; however, the bank continues to report weak operating metrics, coupled with elevated slippages, Although SMA-2 portfolio declined qoq and incremental slippages will come down in FY18, but there is a risk of hair cut due to resolution in various NPAs, which we believe will keep credit cost elevated in FY18. Thus adding pressure on the return ratios in FY18, thus overshadowing cheap valuations. The stock currently trades at 1.5/1.25x our FY18/FY19 ABVPS of Rs 210/256 (factoring Rs60 per share of subsidiary and associates). We maintain our Neutral rating on the stock with a revised PT of Rs 320.

Neutral (Maintain)

CMP RS 380/ TARGET RS 320 (-16%)

COMPANY DATA

O/S SHARES (MN) :	543
MARKET CAP (RSBN) :	157
MARKET CAP (USDBN) :	2.3
52 - WK HI/LO (RS) :	339 / 156
LIQUIDITY 3M (USDMN) :	15.2
PAR VALUE (RS) :	10

SHARE HOLDING PATTERN, %

	Sep 16	Jun 16	Mar 16
FII / NRI :	66.3	66.3	66.3
FI / MF :	6.0	6.4	6.2
NON PRO :	20.5	20.2	19.6
PUBLIC :	0.8	0.8	1.0
GOVT :	6.4	6.3	7.0

Key Financials

Rs mn	FY17	FY18E	FY19E
Pre-prov ROE (%)	31.7	30.6	30.3
Pre-prov ROA (%)	1.6	1.5	1.5
Net Profit	14,816	24,569	41,176
% growth	NA	65.8	67.6
Adj BVPS (Rs)	184.0	250.3	324.2
ROE (%)	5.4	8.2	12.3
P/E (x)	10.8	6.6	4.0
Adj P/BV (x)	1.49	1.10	0.85
EPS (Rs)	25.6	41.5	68.2

CHANGE IN ESTIMATES

Rs bn	Revised Est.		% Revision	
	FY18E	FY19E	FY18E	FY19
NII	99.0	119.4	2.5	7.8
PPP	86.7	91.8	26.6	19.2
Core PAT	14.8	24.6	-8.0	-2.9
EPS (Rs)	25.5	40.3	-8.2	-2.8

Manish Agarwalla, Pradeep Agrawal, Pares Jain

(Rs bn)	Q4FY17	Q4FY16	yoy %	Q3FY17	qoq %	vs. expect. %	Comments
Net interest income	27.1	23.7	14.1	24.1	12.2	3.7	NII improved due to marginal pick up in loan growth.
NIM (%)	2.2	2.2	4bps	2.2	4bps	(7bps)	Below expectation due to higher NPAs, but improved due to
Advances	3420.1	3247.1	5.3	3316.4	3.1	0.1	Marginal pick up was due to growth in SME (11.4%), Agri (10.3%), retail (9%)
Corporate advances	1347.2	1367.8	-1.5	1347.6	0.0		Corporate advances continued to remain weak
Retail advances	589.1	540.7	9.0	549.8	7.2		Educational loan 13.5% yoy; personal loan 15% yoy, vehicle loan 19% yoy
Deposit	4952.8	4797.9	3.2	5103.3	-2.9		Term deposits declined 3% yoy, CASA deposits grew 21% yoy
CASA	1497.5	1235.4	21.2	1537.1	-2.6		Savings and Demand deposit grew 22.6% and 13.9% respectively
CASA %	0.0	27.4 (2738bps)		32.1 (3212bps)			CASA will continue to grow to 35% by FY18
Core fee	4.8	4.4	7.7	5.3	-10.2	-10.0	Fee income driven by sale of PSL certificate (Rs 850 mn)
Trading gain	12.7	3.4	278.3	7.5	70.1		
Operating expenses	21.3	21.1	1.0	22.2	-4.2	-3.4	Employee expenses declined 4.5% yoy, other opex grew 8.8% yoy
Cost to income ratio (%)	55.6	61.7 (609bps)		64.3 (871bps)			
Provision	27.1	63.3	-57.2	14.8	82.5	80.6	NPA Rs 29.2bn; invest. Rs 450mn, std. Rs 290mn, rest. & others Rs-2.9bn
PAT	2.1	-39.1	NA	3.2	-33.5	-66.7	Pat was below estimate due to higher provisions
Slippage	31.0	146.0	-78.8	22.3	39.3		Slippages from restructured loans Rs 9bn
GNPA	9.6	9.4	23bps	10.0	(34bps)		GNPA was contained due to high write off (Rs 24.7bn)
NNPA	6.3	6.4	(9bps)	6.7	(39bps)		PCR ratio improved 310bps qoq to 55.62%
Tier 1 Capital %	9.8	8.8	97bps	9.0	76bps		Tier-1 improved due to rights issue.

Result Update

(Rs mn)	Q4FY17	Q4FY16	YoY growth	Q3FY17	QoQ growth
Interest earned	1,04,929	1,07,329	-2.2	1,02,877	2.0
Interest expended	77,847	83,592	-6.9	78,739	-1.1
Net interest income	27,082	23,738	14.1	24,138	12.2
Net interest margins	2.23	2.19	0.0	2.19	0.0
Non-interest income	23,963	13,832	73.2	17,917	33.7
Total Income	51,045	37,570	35.9	42,055	21.4
Total operating expenses	21,316	21,104	1.0	22,242	-4.2
Payroll costs	11,842	12,395	-4.5	13,057	-9.3
Others	9,473	8,709	8.8	9,184	3.1
Pre-provision Profit	29,729	16,466	80.6	19,813	50.0
Provisions & Contingencies	27,087	63,315	-57.2	14,846	82.5
% Operating income	91.1	384.5	-293.4	74.9	16.2
PBT	2,642	-46,850	-105.6	4,968	-46.8
Provision for Taxes	500	-7,795	-106.4	1,749	-71.4
% of PBT	18.9	16.6	2.3	35.2	-16.3
Net Profit	2,142	-39,055	-105.5	3,219	-33.5
Equity	5,973	5,430	10.0	5,430	10.0
EPS, Rs	3.6	-71.9	-105.0	5.9	-39.5
Advances	34,20,088	32,47,148	5.3	33,16,364	3.1
Deposits	49,52,752	47,97,916	3.2	51,03,275	-2.9
Advances / Deposits (%)	69.1	67.7	1.4	65.0	4.1
Gross NPAs	3,42,020	3,16,378	8.1	3,43,387	-0.4
Gross NPAs (%)	9.6	9.4	0.2	10.0	-0.3
Net NPAs	2,16,490	2,08,329	3.9	2,22,958	-2.9
Net NPAs (%)	6.3	6.4	-0.1	6.7	-0.4
CAR – Total	12.9	11.1	1.8	12.3	0.6

Source: Company, PhillipCapital India Research

Financials

Income Statement

Y/E Mar, Rs mn	FY16	FY17	FY18e	FY19e
Interest on Loans	313,773	295,857	315,087	352,898
Interest on Investments	114,078	107,113	114,611	126,072
Others	12,371	10,907	11,561	12,255
Total Interest Earned	440,221	413,876	441,259	491,225
Total Interest Expended	342,588	315,159	329,660	363,435
Net Interest Income	97,634	98,718	111,600	127,790
Total noninterest income	48,752	75,540	67,811	65,813
Total Income	146,386	174,258	179,411	193,603
Personnel Expenses	44,459	49,151	54,066	59,473
Other Expenses	30,461	35,972	39,317	43,462
Total Op expenses	74,919	85,123	93,383	102,935
Net Inc (Loss) before prov	71,467	89,135	86,029	90,668
Provision and coningencies	103,324	67,520	60,410	57,594
Net Inc (Loss) before tax	-31,858	21,615	25,619	33,073
Provision for Income Tax	-3,730	5,200	5,636	7,276
Net Profit	-28,128	16,415	19,983	25,797

Balance Sheet

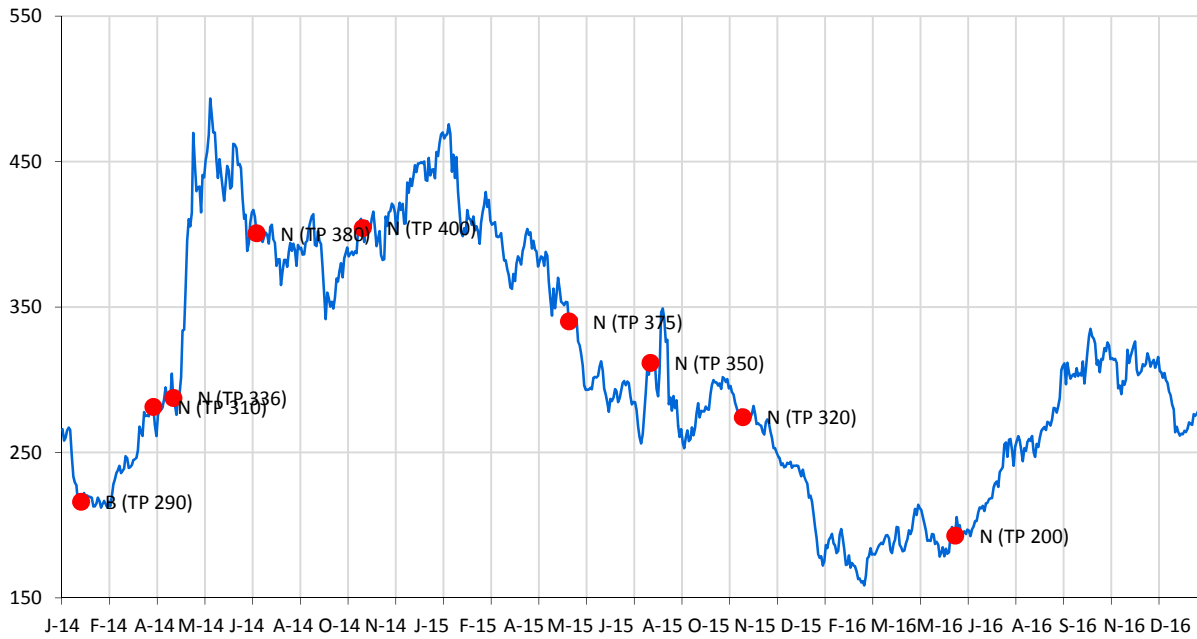
Y/E Mar, Rs mn	FY16	FY17	FY18e	FY19e
Assets				
Cash & Bal with RBI	567,337	588,255	652,963	724,788
Loans, Adv & Int accrued	3,247,148	3,420,088	3,762,096	4,205,695
Investments	1,423,093	1,502,659	1,647,420	1,820,689
Fixed Assets (Net)	71,981	71,683	78,851	86,737
Other assets	220,049	252,518	257,266	269,155
Total Assets	5,529,608	5,835,202	6,398,596	7,107,064
Liabilities				
Share capital	5,430	5,973	6,078	6,167
Reserves and Surplus	256,155	277,151	299,570	325,578
Borrowing	163,733	256,036	294,441	338,607
Total Deposits	4,797,916	4,952,760	5,410,350	6,010,247
Other liab incld prov	146,927	150,551	165,606	182,167
Total Liabilities	5,529,608	5,835,202	6,398,596	7,107,064

Source: Company, PhillipCapital India Research Estimates

Valuation Ratios

	FY16	FY17	FY18e	FY19e
Earnings and Valuation Ratios				
Pre-provision Operating RoAE (%)	27.2	32.7	29.2	28.4
RoAE (%)	(10.7)	6.0	6.8	8.1
Pre-provision Operating ROA (%)	1.3	1.6	1.4	1.3
RoAB (%)	(0.54)	0.31	0.35	0.40
EPS (Rs.)	(51.8)	27.5	32.9	41.8
Dividend per share (Rs.)	0.0	0.0	2.0	5.0
Book Value (Rs.)	481.7	474.0	502.9	537.9
Adj BV (Rs.)	151.0	163.7	210.4	256.7
Revenue Analysis				
Interest income on IBA (%)	8.4	7.7	7.6	7.7
Interest cost on IBL (%)	6.8	6.1	5.9	5.9
NIM on IBA / AWF (%)	1.9	1.8	1.9	2.0
Core fee Inc / AWF (%)	0.3	0.4	0.4	0.4
Portfolio gains / Total Inc (%)	7.3	20.6	9.1	4.3
Op.Exp / TI (%)	54.9	58.9	56.8	55.5
Op.Exp / AWF (%)	1.4	1.6	1.6	1.6
Employee exps / Op exps (%)	59.3	57.7	57.9	57.8
Tax / Pre-tax earnings (%)	11.7	24.1	22.0	22.0
Asset Quality				
GNPAs / Gr Adv (%)	9.4	9.6	9.0	8.3
NNPAs / Net Adv (%)	6.4	6.3	5.5	4.7
Growth Ratio				
Loans (%)	(1.6)	5.3	10.0	11.8
Investments (%)	(2.1)	5.6	9.6	10.5
Deposits (%)	0.9	3.2	9.2	11.1
Networth (%)	(0.8)	6.6	6.7	7.3
Net Int Income (%)	1.0	1.1	13.0	14.5
Non-fund based income (%)	14.2	17.7	15.5	9.5
Non-Int Exp (%)	3.1	13.6	9.7	10.2
Profit Before Tax (%)	(191.1)	(167.8)	18.5	29.1
Net profit (%)	(204.1)	(158.4)	21.7	29.1
Asset / Liability Profile				
Avg CASA/ Deposits (%)	24.8	28.0	30.5	30.7
Avg Adv / Avg Dep (%)	63.9	61.6	62.6	63.5
Avg Invst / Avg Dep (%)	30.1	30.0	30.4	30.4
Incr Adv / Deposits (%)	(125.5)	111.7	74.7	73.9
Avg Cash / Avg Dep (%)	11.0	11.9	12.0	12.1
Capital Adequacy Ratio:				
Tier I (%)	11.1	12.9	13.0	12.9
	8.8	9.8	9.8	9.7
Internal Capital Generation rate (%)	8.2	8.9	8.7	8.4
NNPAs to Equity (%)	65.9	64.3	57.2	51.8

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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