

# Union Bank of India

CMP: ₹ 207

TP: ₹ 220

Accumulate

## High Points

- NII and Operating profit slightly higher than our estimates
- Unexpected jump in NPV loss in restructured loan book
- Sharp decline in slippage ratio
- Higher NPL provisioning and investment depreciation losses dent bottom-line
- View: Cut our Rating to Accumulate with a target price of ₹220

## Scrip Details

|                    |             |
|--------------------|-------------|
| Equity             | ₹ 6353mn    |
| Face Value         | ₹ 10/-      |
| Market Cap         | ₹ 131.5bn   |
|                    | USD 2.5bn   |
| 52 week High / Low | ₹ 359 / 156 |
| Avg. Volume (no)   | 1,785,069   |
| BSE Sensex         | 17,077      |
| NSE Nifty          | 5,158       |
| Bloomberg Code     | UNBK IN     |
| Reuters Code       | UNBK.BO     |

Core interest income and Operating profit slightly higher than our estimates but much higher NPV losses on restructured loan book and NPL provisioning dent bottom-line

- In Q3 FY12, the Union Bank of India's (UBI) net interest income (NII) grew 10% YoY to ₹ 17.8bn — 4.2% higher than our estimates of ₹ 17.1bn. It reported operating profit of ₹ 12.8bn compared to our estimates of ₹ 12.4bn. Bottom-line de-grew by 66% YoY to ₹ 2bn (compared to our estimates of ₹ 6bn) and consensus estimates of ₹ 5.4bn.
- Contained cost of funds on the back of moderate business growth, higher incremental C-D ratio and higher yield on funds aided margin. The bank's margin increased by 10bps to 3.31% compared to 3.21% in Q2 FY12 though lesser than previous year corresponding period margin at 3.44%.
- The deviation in bottom-line was mainly due to much higher overall provisions. On fresh restructuring, NPV loss provision was much higher than expectation at ₹ 3.8bn. Apart from that, there was much higher provision for bad-debts at ₹ 4.2bn and higher investment depreciation losses of ₹ 730mn. On sequential basis, gross slippages came down sharply to 1.6% from 5.3% in Q2 FY12 and 2.24% in Q1 FY12; a positive surprise.
- On core income level and operating level, the bank's Q3 FY12's financial performance were slightly higher than our estimates. But, much higher than expected provisioning was a negative surprise which resulted into deviation at net profit level. We reduce our FY12 and FY13 earnings estimates by 4.5% and 5% respectively and reduce our target price by 8% to ₹ 220. At current price, the stock quotes at 1.0x ABV FY13. We cut our stock rating to **Accumulate** due to reduction in our earning estimates and recent rally in stock price.

## Q3FY12 Result (₹ mn)

| Particulars                 | Q3FY12 | Q2FY12 | Q3FY11 | QoQ(%) | YoY(%) | 9MFY12  | 9MFY11  | YoY(%) |
|-----------------------------|--------|--------|--------|--------|--------|---------|---------|--------|
| Interest Income             | 53,747 | 51,104 | 41,995 | 5.2    | 28.0   | 154,009 | 118,374 | 30.1   |
| Interest Expenditure        | 35,939 | 34,492 | 25,836 | 4.2    | 39.1   | 103,686 | 73,377  | 41.3   |
| Net interest income         | 17,809 | 16,612 | 16,158 | 7.2    | 10.2   | 50,323  | 44,997  | 11.8   |
| Other operating income      | 5,921  | 5,009  | 4,936  | 18.2   | 20.0   | 15,770  | 14,382  | 9.6    |
| Total Net Income            | 23,730 | 21,622 | 21,094 | 9.8    | 12.5   | 66,093  | 59,379  | 11.3   |
| Overheads                   | 10,889 | 9,571  | 8,483  | 13.8   | 28.4   | 29,543  | 25,025  | 18.1   |
| Operating profit            | 12,841 | 12,051 | 12,611 | 6.6    | 1.8    | 36,550  | 34,354  | 6.4    |
| Tax                         | 1,144  | 2,297  | 2,816  | (50.2) | (59.4) | 6,172   | 7,549   | (18.2) |
| Provisions                  | 9,727  | 6,228  | 4,000  | 56.2   | 143.2  | 20,245  | 11,961  | 69.3   |
| Net profit                  | 1,970  | 3,525  | 5,796  | (44.1) | (66.0) | 10,133  | 14,844  | (31.7) |
| Equity Capital              | 6,353  | 6,353  | 5,051  |        | 25.8   | 6,353   | 5,051   | 25.8   |
| EPS ( in unit INR)          | 3.8    | 6.7    | 11.5   | (44.0) | (67.2) | 40.7    | 39.7    | 2.5    |
| Gross Non Performing Assets | 52,089 | 51,364 | 35,809 | 1.4    | 45.5   |         |         |        |
| Net Non Performing Assets   | 28,789 | 29,589 | 15,974 | (2.7)  | 80.2   |         |         |        |
| Gross NPAs (%)              | 3.3    | 3.5    | 2.7    | (0.2)  | 0.7    |         |         |        |
| Net NPAs (%)                | 1.9    | 2.0    | 1.2    | (0.2)  | 0.7    |         |         |        |
| RoA (%)                     | 0.4    | 0.6    | 1.2    |        |        |         |         |        |

## Financials

| Year  | NII    | PPP    | NP     | NIM(%) | BV (₹) | ABV (₹) | RoAA (%) | RoAE (%) | P/B (x) | P/ABV (x) | P/E (x) |
|-------|--------|--------|--------|--------|--------|---------|----------|----------|---------|-----------|---------|
| FY10  | 41,924 | 36,593 | 20,749 | 2.4    | 174    | 160     | 1.2      | 21.7     | 1.2     | 1.3       | 5.0     |
| FY11  | 62,162 | 43,050 | 20,799 | 3.0    | 211    | 187     | 1.0      | 18.0     | 1.0     | 1.1       | 5.2     |
| FY12E | 69,881 | 51,088 | 17,884 | 2.8    | 237    | 198     | 0.7      | 13.4     | 0.9     | 1.0       | 6.1     |
| FY13E | 76,552 | 53,005 | 18,801 | 2.7    | 265    | 209     | 0.6      | 12.8     | 0.8     | 1.0       | 5.8     |

Figures in ₹ mn

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**Moderate business growth:** The bank's total business grew 12.8% YoY to ₹ 3.6tn; deposits and net advances grew 10% and 16.9% to ₹ 2.1tn and ₹1.5tn respectively. The bank's business growth is in-line with our expectations. Higher credit mobilization than deposit growth led to 440bps YoY and 77bps QoQ rise in its Credit-deposit ratio to 76.1% as against 71.7% in Q3 FY11 and 75.3% in Q2 FY12. On the deposits side, CASA share slightly rose to 32.5% from 32.1% in end-Q2 FY12 and decline from 33.3% in end-Q3 FY11.

In FY12, the management expects 16% deposit growth and 16-18% credit book growth. We expect deposits and credit book growth at 16.5% and 16.3% respectively in FY13.

**Sequential rise in margin:** On liability front, moderate business growth improved CASA share and contained liabilities costs. On asset side, higher C-D ratio and higher yield aided margin. The bank expanded margin to 3.31% from 3.21% in Q2 FY12. For FY12, the management expects margins of 3.2% compared to 3.33% (on fortnightly average basis) in FY11. We estimate the bank's margins to drift by 13 bps in FY12 to 2.84% and further by 14 bps 2.7% (on yearly average basis) in FY13.

**Higher Non-fund income:** The other income increased by 20% YoY to ₹ 5.9bn primarily, on account of higher recoveries (3 times jump to ₹ 900mn) and 16% YoY growth in core non-interest income to ₹ 3.2bn. Going forward in Q4 FY12, the bank is expected to perform well on treasury income front with fall in bond yields.

**Higher provisioning dents overall profitability:** In Q3 FY12, the bank's NPL provisioning increased by 33% to ₹ 5.3bn (including ₹ 1bn for standard assets) compared to ₹ 4bn in Q3 FY11 and ₹ 5bn in Q2 FY12. Though, slippages ratio came down sharply on YoY and QoQ basis. The bank's GNPA increased marginally on sequential basis to ₹ 52bn. Higher NPL provisioning also reflected into improvement in provision coverage to 63% (including technical write-offs) and higher decrease in NNPA ratio. In Q3 FY12, bank's credit cost increased to 1.45% as against 1.32% in Q3 FY11. However, it was stable on sequential basis.

Higher than expected provisioning of ₹ 3.8bn for NPV loss on fresh restructuring of a telecom loan account of ₹ 20bn led to deviation on bottomline level.

Further, bank had provided ₹ 730mn as against 60mn in Q3FY11 on account of investment depreciation losses.

**Asset quality comfortable as of now but future could unfold negative surprises:** As on end-Q3 FY12, the bank's gross NPAs and net NPAs rose by 45% YoY and 80% YoY to ₹ 52.1bn and ₹ 28.8bn respectively. Gross NPA ratio and Net NPA ratio rose by 65bps and 67bps on YoY basis to 3.33% and 1.88% respectively. However, there was sequential decline of 16bps in each of the ratios. On sequential basis, gross slippages came down sharply to 1.6% from 5.3% in Q2 FY12 and 2.24% in Q1 FY12. In fact, the bank's asset quality has shown improvement on sequential basis.

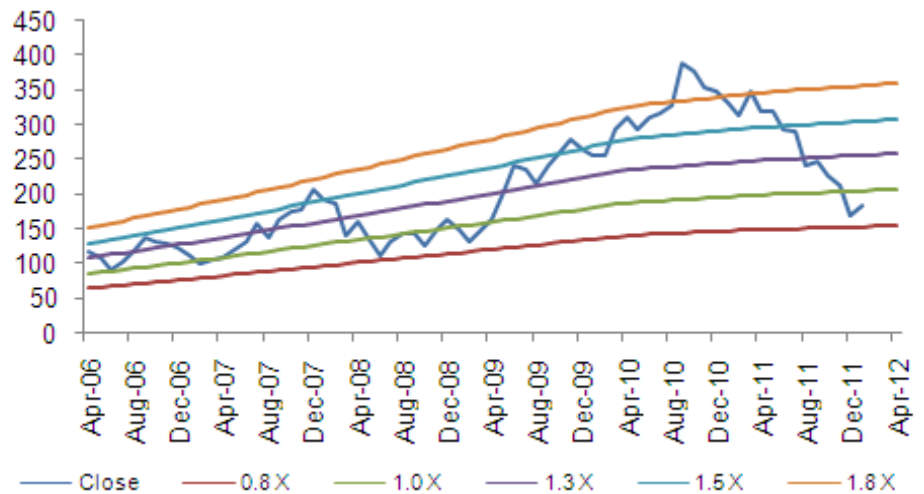
The restructured loans as on end-Q3 FY12 were at ₹ 86bn. The loans of around ₹32bn was expected to be restructured in 2H FY12, out of which ₹ 20bn was already restructured in Q3 FY12, the rest amount of ₹ 12bn would come for restructuring in Q4FY12.

**Branch Network Expansion:** The bank opened 39 branches and 268 ATMs in Q3 FY12, taking the total branch network to 3177 branches and 3025 ATMs. The management plans to add 225 branches (including 100 FI) and increase the ATMs to 4000 in this fiscal.

### Valuation

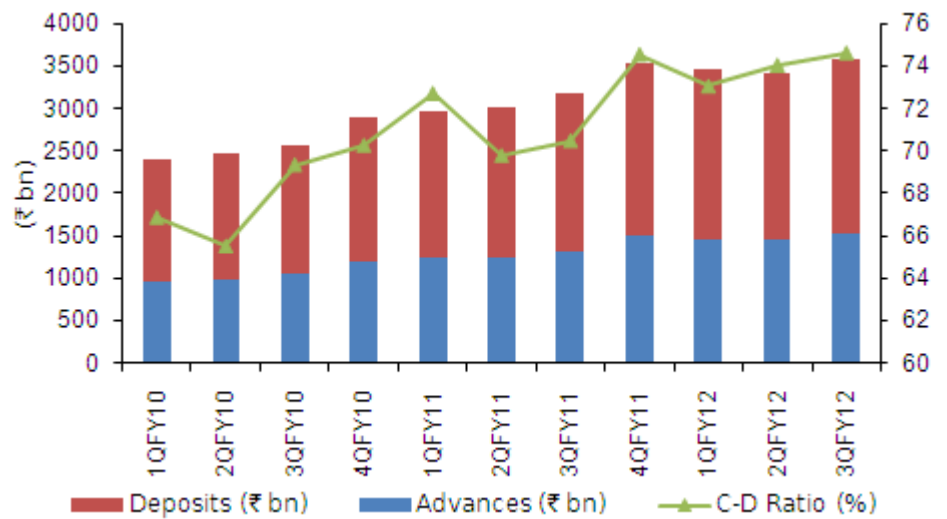
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### Union Banks's P/BV Chart



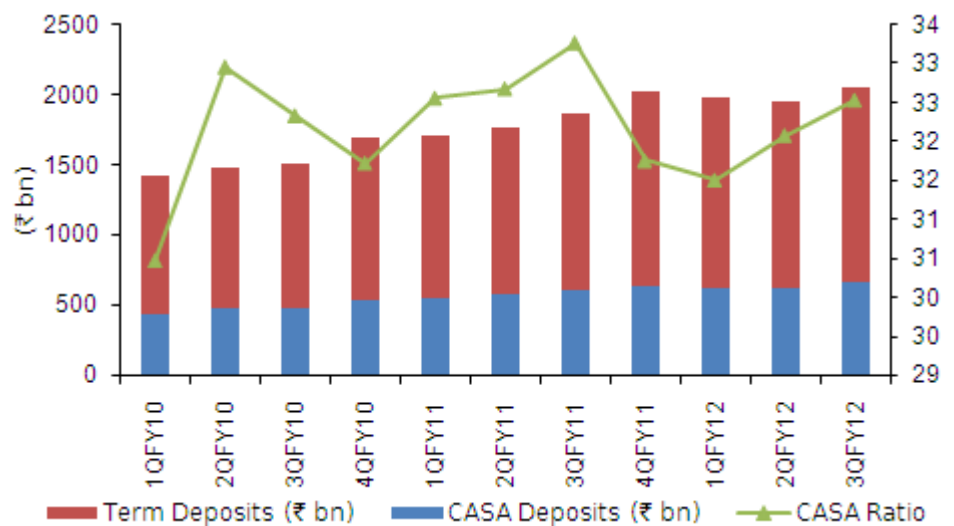
Source: Capitaline, Dolat Research

**Union Bank's Business mix**



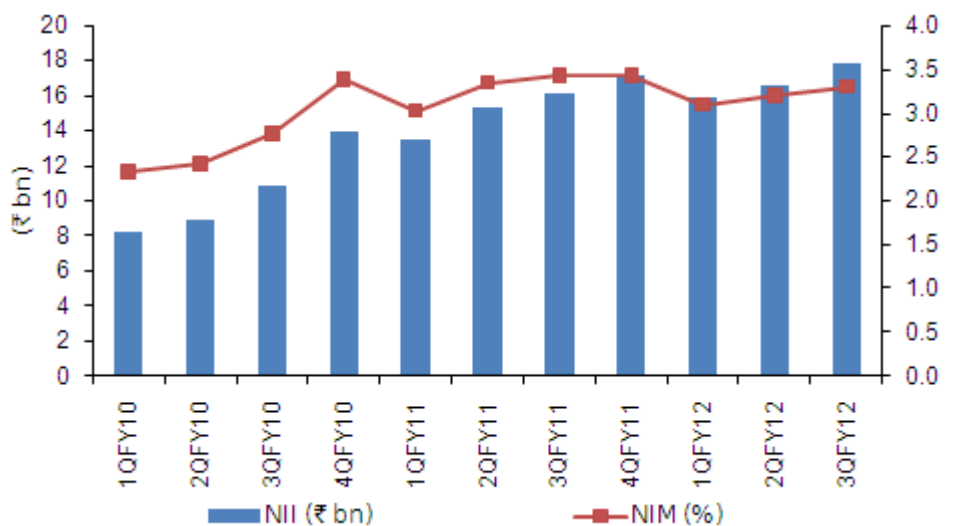
Source: Banks, Dolat Research

**Union Bank's Deposit Profile**



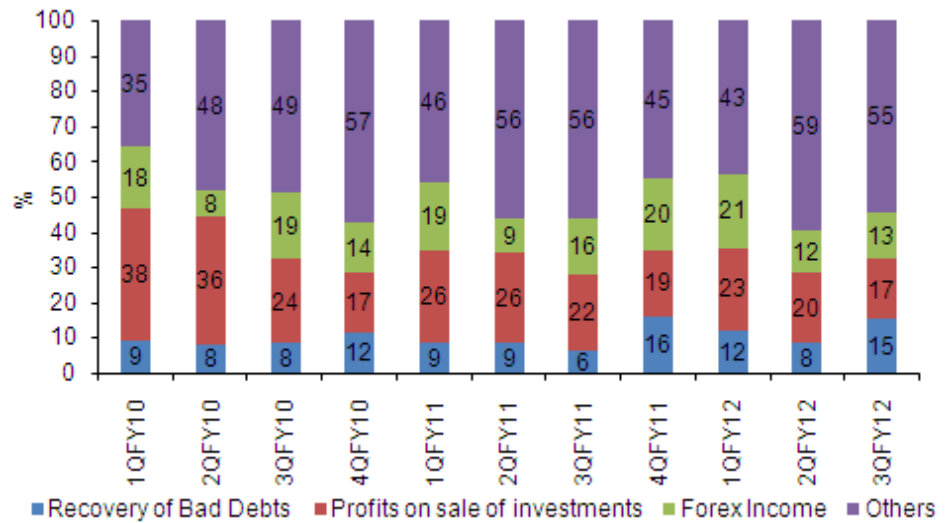
Source: Banks, Dolat Research

**Union Bank's NII & NIM (%)**



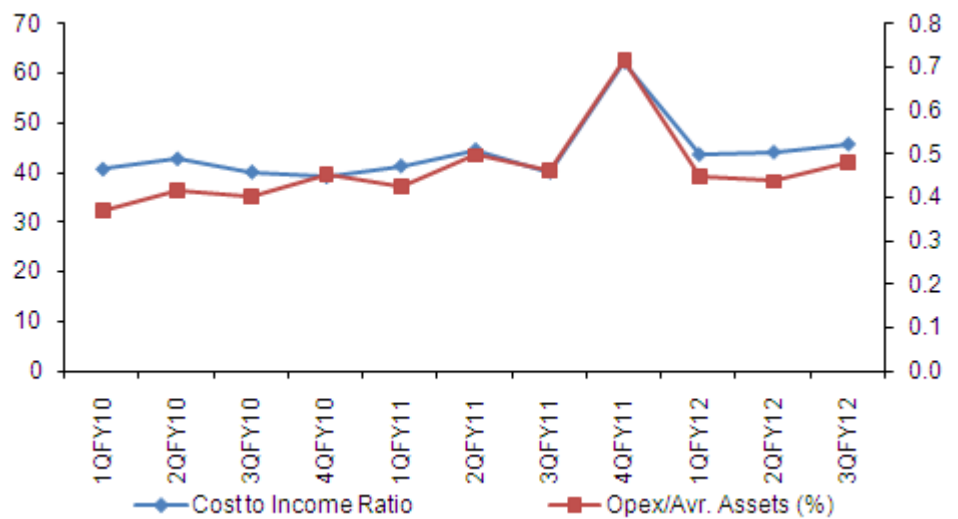
Source: Banks, Dolat Research

**Union Bank's Other income break-up (%)**



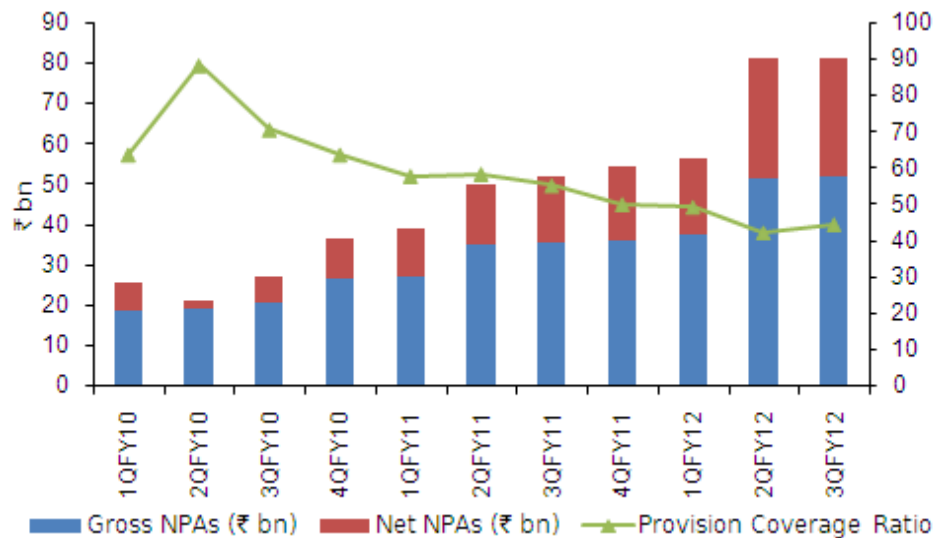
Source: Capitaline, Dolat Research

**Union Bank's Operating Cost Structure (%)**



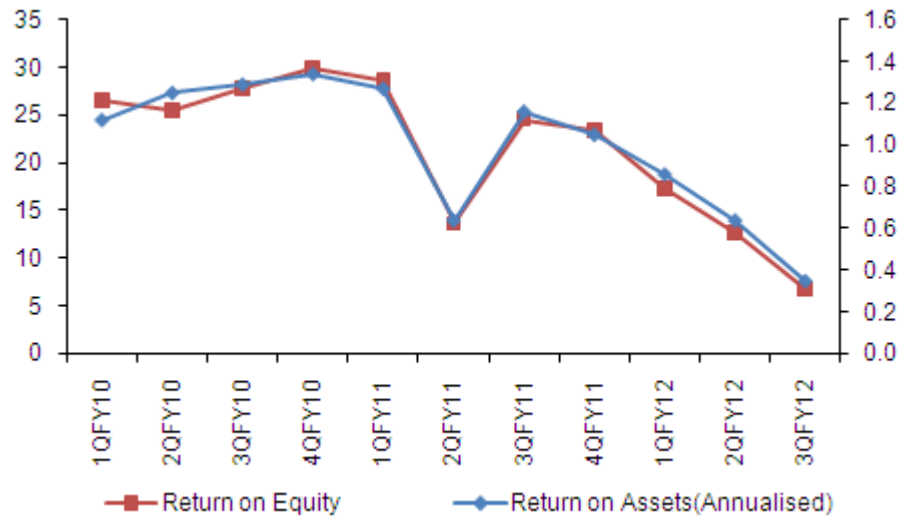
Source: Banks, Dolat Research

**Union Bank's Asset Quality**



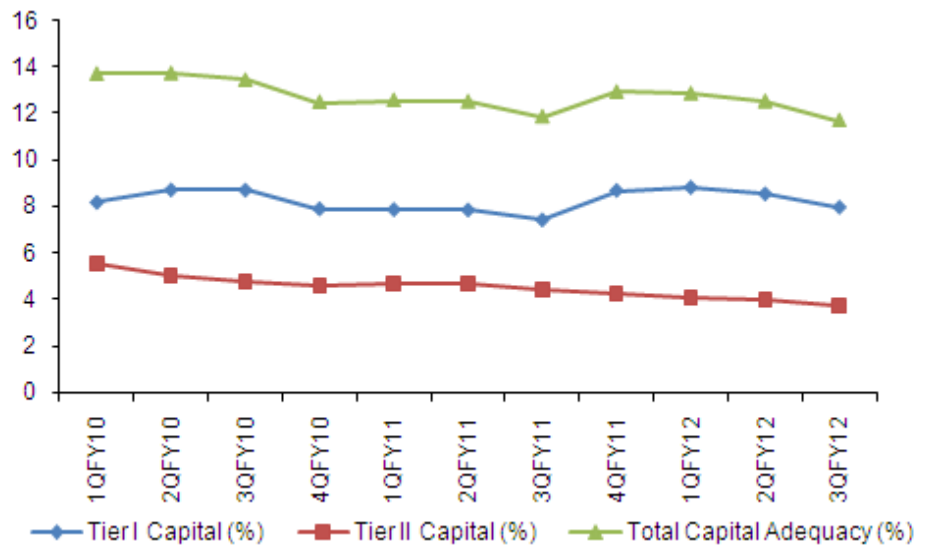
Source: Banks, Dolat Research

**Union Bank's Return Ratios (%)**



Source: Capitaline, Dolat Research

**Union Bank's Capital Adequacy (%)**



Source: Banks, Dolat Research



|            |                               |
|------------|-------------------------------|
| BUY        | Upside above 20%              |
| ACCUMULATE | Upside above 5% and up to 20% |
| REDUCE     | Upside up to 5%               |
| SELL       | Negative Returns              |

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