RBL Bank

23 October 2019

2QFY20 Result Update

Reuters: RATB; Bloomberg: RBK IN

RBL accelerates NPA recognition and makes excess provision

RBL Bank (RBL) reported 2QFY20 results with the key pointers being: (1) Gross slippages spiked to Rs 13.77bn of which Rs 8bn were accelerated slippages from corporate stress pool (2) Loan growth slowed to 27% YoY and core fee income growth also slowed to 19% YoY (3) NIM expansion journey continued with NIM at 4.35%, up 4 bps QoQ and 27 bps YoY (4) Opex growth was 41% YoY due to continued investment in retail franchise (See *comprehensive* conference call takeaways on page 2 for *significant incremental colour*). Per se, on the key P&L items, RBL posted 6% YoY NII growth at Rs8,687mn, PPOP growth of 42% YoY at Rs6,358mn and PAT decline of 73% YoY at Rs543mn. We have revised our estimates for FY20/FY21/FY22 and retained Buy rating on RBL, revising our target price to Rs389 (from Rs463 earlier) and valuing the stock at 1.5x H1FY22E P/BV.

Gross slippages spiked to Rs 13.77bn of which Rs 8bn were accelerated slippages from corporate stress pool: RBL raised the size of its corporate stress pool to ~Rs 18bn (from ~Rs 13bn earlier) and stated that Rs 8bn of this pool were taken as slippages on the conservative principle of inherent weakness. There was also a technical slippage of ~Rs 2.5bn that slipped but was upgraded within the quarter and is not likely to slip again. The provision made on the Rs 8bn slippage amounted to ~Rs 3.5bn which is in excess of regulatory requirement. Management stated that its intention is to clean up the books by the end of the fiscal and primarily by 3QFY20. Following the cleanup, a relatively normalized gross slippage of Rs 2-2.5bn per quarter can be expected.

Loan growth slowed to 27% YoY and core fee income growth also slowed to 19% YoY: Wholesale book grew just 12% YoY and now forms 52% of total book. Within wholesale, commercial banking was flat YoY whereas corporate loan book grew 18% YoY. Non wholesale loans grew 49% YoY driven by retail loans, which grew 62% YoY. Retail loan growth, in turn was driven by LAP and credit cards, which grew 61% and 121% YoY respectively. Micro banking book grew 31% YoY.

NIM expansion journey continued with NIM at 4.35%, up 4 bps QoQ and 27 bps YoY: The key aspects driving this expansion was strong growth in high-yielding sub-segments of non-wholesale book viz. (i) micro banking and (ii) credit cards. Wholesale yield was down 20 bps QoQ to 9.2%, likely a consequence of slower commercial book growth, but was still up 60 bps YoY. Non wholesale yield was at 15.4%, up 130 bps YoY due to mix change.

Opex growth was 41% YoY due to continued investment in retail franchise: The target is to take branch count to 380-400 by the end of the fiscal year and associated cost would accrue. The credit card business, which is growing fast, has upfront cost and therefore had a concomitant impact on opex rise.

Valuation and outlook: We have revised our NII estimates by -1.5%/-3.2%/-3.7%, PPOP estimates by -3.1%/1.3%/2.4% and PAT estimates by -10.0%/-5.2%/-4.5% for FY20/FY21/FY22, respectively. We have retained Buy rating on RBL, revising our target price to Rs389 (from Rs463 earlier) and valuing the stock at 1.5x H1FY22E P/BV.

BUY

Sector: Banking

CMP: Rs287

Target Price: Rs389

Upside: 36%

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Key Data

Current Shares O/S (mn)	430.5
Mkt Cap (Rsbn/US$bn)	122/1.7
52 Wk H / L (Rs)	717/241
Daily Vol. (3M NSE Avg.)	14,497,850

Price Performance (%)

	1 M	6 M	1 Yr
RBL Bank	(26.0)	(58.4)	(39.6)
Nifty Index	2.8	(1.4)	12.5

Source: Bloomberg

Y/E March (Rsmn)	2QFY20	2QFY19	1QFY20	YoY (%)	QoQ (%)
Interest income	21,262	14,634	20,227	45.3	5.1
Interest expenses	12,575	8,705	12,054	44.5	4.3
Net interest income	**8,687**	**5,930**	**8,173**	46.5	6.3
NIM (%)	***4.35***	***4.08***	***4.31***	27 bps	4 bps
Non-interest income	4,415	3,331	4,812	32.5	(8.2)
Total income	**13,102**	**9,261**	**12,985**	41.5	0.9
Staff costs	1,961	1,509	1,845	29.9	6.2
Other operating expenses	4,783	3,261	4,952	46.7	(3.4)
Total operating expenses	6,744	4,770	6,797	41.4	(0.8)
Cost- to-income (%)	*51.5*	*51.5*	*52.3*	-4 bps	-87 bps
Pre-provisioning operating profit	**6,358**	**4,491**	**6,188**	41.6	2.8
Provisions	5,333	1,397	2,132	281.8	150.2
PBT	**1,025**	**3,094**	**4,056**	(66.9)	(74.7)
Tax	482	1,048	1,386	(54.0)	(65.2)
-Effective tax rate	47.0	33.9	34.2	1314 bps	1286 bps
PAT	**543**	**2,045**	**2,671**	(73.4)	(79.7)
EPS (Rs)	1.3	4.8	6.3	(74.0)	(79.8)
BV (Rs)	176.7	163.4	177.1	8.2	(0.2)
Deposits	628,291	477,901	608,109	31.5	3.3
Advances	584,761	458,727	568,367	27.5	2.9

Source: Company, Nirmal Bang Institutional Equities Research

Comprehensive Conference Call Takeaways

Asset Quality

- Credit challenges pertaining to the bank will be fully absorbed in Q3FY20.
- Given the macros, the increase in stress levels at the bank has been more than what the bank had anticipated. This is also due to slower pace of resolutions and poor coordination amongst various banks.
- The bank stated it has reviewed its exposure in greater detail and has become more conservative in terms of recognition of stress and provisioning.
- Of the total Rs. 18 bn worth of stress pool identified by the bank, Rs. 8 bn has slipped into NPA during Q2FY20. The bank has provided Rs. 3.5 bn against this slippage. The rest of the slippage is expected to come in Q3FY20.
- The bank stated that the stress it is seeing its specific only to certain corporates. It does not see any stress with any of other sectors perceived as risky such as NBFCs, including HFCs, infra and real estate. In these sectors, the bank has low instances of SMA1 and SMA2.
- The bank does not have any exposure to project finance.
- SMA1 and SMA2 stand at 0.45% and 0.39%, respectively. Adjusting for the identified stressed accounts in the loan portfolio, SMA1 and SMA2 are 0.31% and 0.22%, respectively.
- The bank has conducted its own research and analysis with respect to retail slippages and asset quality issues emanating from slowing down of economy and threat of job losses. The bank stated that its portfolio continue to be stable in terms of delinquencies and early warning signals as well. Even with respect to other banks, on comparative basis, the bank's retail asset quality is stable.
- The bank has tightened underwriting criteria and has been avoiding high risk loans. New acquisitions have been cut by 15-20% and the sales team has been aligning to the new underwriting criteria and finding other ways to grow. As a result, card acquisition rate has come down.
- In the LAP segment, the bank had always been cautious in terms of customer segments as well as collateral. The bank has further tightened its norms with respect to LAP loans, keeping in mind the stretched working capital positions in the small business segment.
- In the micro banking segment, the overall market is steady. Collections in the flood affected areas have held up and should improve in another 4-6 months. Further, the bank's concentration in top states, in the microfinance space, is far lower than peers'. The bank is also keeping a watch on ticket sizes, which is already lower than peers'.
- In the total slippages, Rs. 2.5-2.75 bn was a technical slippage comprising of just one account. This account got upgraded to standard in the same quarter. Apart from this, there was an agri slippage of about Rs. 0.70 bn.
- In terms of exposure to a stressed HFC, the bank's exposure has reduced since last quarter. Further, the bank has strengthened the security structured with respect to this exposure. Overall, this account is not an issue for the bank.
- Doubling of retail NPAs is a function of changing business mix as unsecured book has been growing.
- The bank stated it has moved to daily recognition of NPAs in the retail portfolio.

Business and Loan Growth

- In terms of profitability, the bank expects to be back to normalized levels by Q4. For FY20, the overall profitability is expected to be lower than last year. It would be about 70-80% of FY19 profitability.

Margin, Liabilities and Liquidity

- Overall yield improved by 15 bps during Q2FY20, largely on account of favourable change in business mix.
- Opening of new branches has helped bank secure more granular CASA deposits. This has also helped the bank avoid high cost bulk deposits.
- During the quarter, the bank was sitting on Rs. 40 bn worth of G-secs since it couldn't deploy the capital given the current demand environment.

Operating Expenses

- The bank is on track to open 380-400 branches by end of FY20.
- The bank stated it would be accelerating its BC branch expansion, largely in the existing districts where it is already present. The intention is to cover villages where microfinance penetration is low.
- Opex growth can be explained by investments being undertaken to open the branches and the hiring associated with that, as well as, growth in the credit card franchise where costs are being taken upfront.

Capital Adequacy

- The bank stated it plans to raise capital within the current year, ie, FY20. For this, it has been getting interest from existing and new investors.

Exhibit 1: Financial summary

Y/E March (Rsmn)	FY18	FY19	FY20E	FY21E	FY22E
Net interest income	17,663	25,395	34,141	43,433	55,515
Pre-provisioning operating profit	13,311	19,398	26,319	33,465	41,203
PAT	6,351	8,670	10,677	14,898	18,727
EPS (Rs)	15.8	20.5	23.8	31.7	39.9
BV (Rs)	159.3	176.9	215.3	242.5	276.6
P/E (x)	18.2	14.0	12.0	9.0	7.2
P/BV (x)	1.8	1.6	1.3	1.2	1.0
Gross NPAs (%)	*1.4*	*1.4*	*3.9*	*3.4*	*3.2*
Net NPAs (%)	*0.8*	*0.7*	*2.1*	*1.1*	*0.9*
RoA (%)	*1.1*	*1.2*	*1.2*	*1.4*	*1.4*
RoE (%)	*11.5*	*12.2*	*12.1*	*13.9*	*15.4*

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 2: Actual performance versus our estimates

(Rsmn)	2QFY20	2QFY19	1QFY20	*YoY (%)*	*QoQ (%)*	2QFY20E	*Devi. (%)*
Net interest income	8,687	5,930	8,173	*46.5*	*6.3*	8,200	*5.9*
Pre-provisioning operating profit	6,358	4,491	6,188	*41.6*	*2.8*	5,436	*17.0*
PAT	543	2,045	2,671	*(73.4)*	*(79.7)*	2,521	*(78.5)*

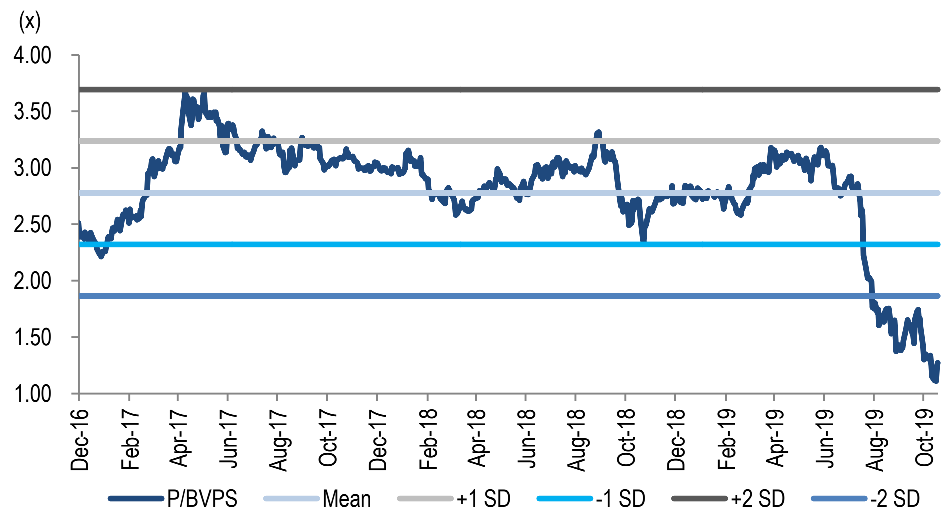
Source: Company, Nirmal Bang Institutional Equities Research N.B. We were expecting a DTA Reduction of Rs 586mn due to which we had also specified a separate adjusted PAT estimate of Rs 1,970mn.

Exhibit 3: Change in our estimates

	Revised Estimate			Earlier Estimate			*% Revision*		
	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	*FY20E*	*FY21E*	*FY22E*
Net Interest Income (Rs mn)	34,141	43,433	55,515	34,677	44,868	57,651	*(1.5)*	*(3.2)*	*(3.7)*
NIMs	4.15	4.27	4.32	4.13	4.23	4.29	*2 bps*	*4 bps*	*3 bps*
Operating Profit (Rs mn)	26,319	33,465	41,203	27,147	33,036	40,255	*(3.1)*	*1.3*	*2.4*
Profit after tax (Rs mn)	10,677	14,898	18,727	11,866	15,716	19,605	*(10.0)*	*(5.2)*	*(4.5)*

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 4: One-year forward P/BV



Source: Company, Nirmal Bang Institutional Equities Research

Financials

Exhibit 5: Income statement

Y/E March (Rsmn)	FY18	FY19	FY20E	FY21E	FY22E
Interest income	45,076	63,007	80,491	100,223	126,976
Interest expenses	27,413	37,612	46,349	56,790	71,460
Net interest income	**17,663**	**25,395**	**34,141**	**43,433**	**55,515**
Fee income	7,226	11,656	14,969	18,877	22,114
Other income	3,456	2,768	3,521	4,231	4,886
Net revenues	28,345	39,818	52,631	66,541	82,516
Operating expenses	15,034	20,420	26,312	33,077	41,313
-Employee expenses	5,507	6,362	7,983	9,962	11,828
-Other expenses	9,527	14,058	18,329	23,115	29,485
Pre-provisioning Operating profit	**13,311**	**19,398**	**26,319**	**33,465**	**41,203**
Provisions	3,178	5,723	12,050	13,556	16,176
-Loan loss provision	2,995	5,234	11,404	12,794	15,236
-Investment depreciation	425	532	646	761	940
-Other provisions	(242)	(43)	0	0	0
PBT	10,133	13,676	14,269	19,909	25,027
Tax	3,782	5,006	3,591	5,011	6,299
PAT	**6,351**	**8,670**	**10,677**	**14,898**	**18,727**

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 7: Balance sheet

Y/E March (Rsmn)	FY18	FY19	FY20E	FY21E	FY22E
Equity capital	4,197	4,267	4,694	4,694	4,694
Reserves & surplus	62,643	71,206	96,375	109,121	125,144
Shareholders' funds	**66,840**	**75,473**	**101,069**	**113,815**	**129,838**
Deposits	**439,023**	**583,944**	**719,715**	**903,005**	**1,144,405**
Borrowings	92,614	118,321	109,582	142,226	184,912
Other liabilities	20,031	25,850	38,537	53,498	72,874
Total liabilities	**618,508**	**803,588**	**968,903**	**1,212,544**	**1,532,030**
Cash/cash equivalent	42,844	66,021	50,914	64,661	82,766
Advances	402,678	543,082	678,853	862,143	1,103,543
Investments	154,475	168,404	212,212	257,923	316,957
Fixed assets	3,340	4,025	4,427	4,870	5,357
Other assets	15,170	22,056	22,497	22,947	23,406
Total assets	**618,508**	**803,588**	**968,903**	**1,212,544**	**1,532,030**

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 6: Key ratios

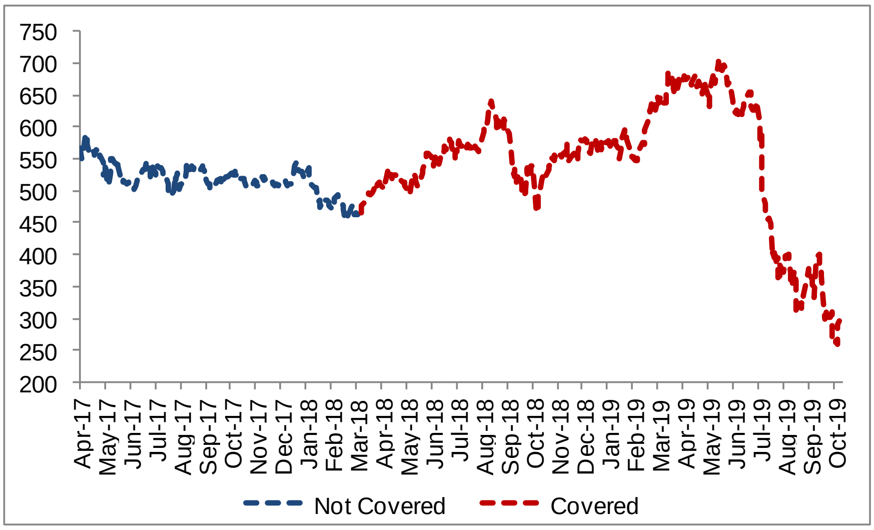
Y/E March	FY18	FY19	FY20E	FY21E	FY22E
Growth (%)					
NII growth	44.6	43.8	34.4	27.2	27.8
Pre-provision profit growth	44.6	45.7	35.7	27.2	23.1
PAT growth	42.4	36.5	23.2	39.5	25.7
Business (%)					
Deposit growth	26.9	33.0	23.3	25.5	26.7
Advance growth	36.7	34.9	25.0	27.0	28.0
Business growth	31.4	33.9	24.1	26.2	27.4
CD	91.7	93.0	94.3	95.5	96.4
CASA	24.3	25.0	27.0	28.5	29.5
Operating efficiency (%)					
Cost-to-income	53.0	51.3	50.0	49.7	50.1
Cost-to-assets	2.7	2.9	3.0	3.0	3.0
Productivity (Rsmn)					
Business per branch	3,176.2	3,478.5	3,586.1	3,922.6	4,495.9
Business per employee	158.8	192.9	201.5	224.1	264.5
Profit per branch	24.0	26.8	27.4	33.1	37.5
Profit per employee	1.2	1.5	1.5	1.9	2.2
Spreads (%)					
Yield on advances	9.8	10.7	10.8	10.8	10.8
Yield on investments	6.9	6.8	7.1	7.0	7.0
Cost of deposits	6.0	6.3	6.2	6.2	6.2
Yield on assets	8.8	9.5	9.8	9.9	9.9
Cost of funds	5.7	6.1	6.1	6.1	6.0
NIM	3.4	3.8	4.1	4.3	4.3
Capital adequacy (%)					
Tier I	13.6	12.1	13.2	11.7	10.4
Tier II	1.7	1.4	1.6	1.4	1.3
Total CAR	15.3	13.5	14.8	13.1	11.7
Asset quality (%)					
Gross NPAs	1.4	1.4	3.9	3.4	3.2
Net NPAs	0.8	0.7	2.1	1.1	0.9
Provision coverage	44.8	50.6	48.3	67.9	71.2
Slippage	1.6	1.5	4.0	2.5	2.5
Credit cost	0.7	1.0	1.8	1.6	1.5
Return (%)					
RoE	11.5	12.2	12.1	13.9	15.4
RoA	1.1	1.2	1.2	1.4	1.4
RoRWA	1.5	1.6	1.6	1.7	1.7
Per share (%)					
EPS	15.8	20.5	23.8	31.7	39.9
BV	159.3	176.9	215.3	242.5	276.6
ABV	151.8	168.1	185.6	222.2	254.4
Valuation (x)					
P/E	18.2	14.0	12.0	9.0	7.2
P/BV	1.8	1.6	1.3	1.2	1.0
P/ABV	1.9	1.7	1.5	1.3	1.1

Source: Company, Nirmal Bang Institutional Equities Research

Rating track

Date	Rating	Market price (Rs)	Target price (Rs)
26 March 2018	Buy	462	579
30 April 2018	Buy	538	628
20 July 2018	Buy	557	649
9 October 2018	Buy	495	647
24 October 2018	Buy	465	652
29 January 2019	Buy	563	675
8 April 2019	Accumulate	671	701
22 April 2019	Accumulate	677	704
8 July 2019	Accumulate	633	696
22 July 2019	Accumulate	500	559
7 August 2019	Buy	364	559
7 October 2019	Buy	303	463
23 October 2019	Buy	287	389

Rating track graph



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