

RBL Bank

7 August 2019

Reuters: RATB; Bloomberg: RBK IN

RBL's corporate lending is no basket case, Upgrade to Buy

We think that the concerns surrounding RBL Bank's (RBL) corporate asset quality are overdone and upgrade the stock to Buy rating. We note that (1) As far as RBL's corporate lending model is concerned, it is highly working capital focused with ~70% of corporate book in short-term working capital category (2) RBL had near negligible exposure to RBI NCLT Lists 1 and 2 (3) Incidence of Divergence with RBI's assessment of asset quality was never cause of any alarm (4) While RBL's exposure to the Williamson Magor group entities and Coffee Day Enterprises is concerning, we believe this is captured in the bank's asset quality guidance for FY20 (5) RBL's digital strategy is best-in-class and typifies the new-age bank RBL has been post current management takeover. We have revised our estimates for FY20/FY21 and upgrade RBL to Buy rating, revising our target price to Rs463 (from Rs559 earlier) and valuing the stock at 1.9x FY21E P/BV.

As far as RBL's corporate lending model is concerned, it is highly working capital focused with ~70% of corporate book in short-term working capital category: RBL's corporate book is known to fully churn in a matter ~18 months. Working capital corporate loans are generally far more straightforward to appraise since cash flows can be more readily forecast over shorter time horizons as opposed to cash flow in long-term projects. We do not, therefore, think that the underlying risk in RBL's corporate book can be very high and we do not see RBL entering a deep NPA cycle as witnessed in ICICI/Axis/Yes.

RBL had near negligible exposure to RBI NCLT Lists 1 and 2: While RBI NCLT Lists 1 and 2 pertain to stressed accounts that belong to a vintage when RBL's book (and lending quantum) was small, the negligible exposure does point to sound lending standards during the previous surge in systemic corporate lending.

Incidence of Divergence with RBI's assessment of asset quality was never cause of any alarm: Divergence in asset quality with RBI's assessment as of FY16 GNPA amounted to 1.6% of FY16 advances. Divergence in FY17 and FY18 did not exceed the prescribed thresholds and hence, required no disclosure from the bank. By and large, RBL does not have a track record that suggests that it has been exercising discretion inappropriately in terms of timely recognition of corporate NPA.

While RBL's exposure to the Williamson Magor group entities and Coffee Day Enterprises is concerning, we believe this is captured in the bank's asset quality guidance for FY20: As per McLeod Russel's FY18 Annual Report, RBL's exposure to the entity is Rs 996mn. As per MCA (ROC) charges data, RBL's sanctions to McNally Bharat could be Rs 2.75bn, assuming no overlap in charges data. As per Coffee Day Enterprises' FY18 Annual Report, RBL's exposure to the entity is also Rs 2.75bn. However, we think that all this is broadly captured in RBL's asset quality guidance of 2-2.5% GNPA and ~1.5% credit costs for FY20. We revise our FY21 credit costs 15 bps higher to 125 bps.

RBL's digital strategy is best-in-class and typifies the new-age bank RBL has been post current management takeover: We met Sameer Singh Jaini, Fintech Expert and Ex-CTO of DCB Bank yesterday and walked away with the key takeaway that RBL's digital strategy is ahead of the curve even when compared with key large banks generally known to have the best digital strategy implementation (See [RBL Bank ahead of even key large banks on digital strategy](#)). We think even greater benefits of opex strategy will be visible after FY21 as the bank is currently in investment phase with regard to technology. We think that RBL can trade at 1.9x FY21E P/BV for FY20/21 RoE profile of 12.8%/15.1%.

Valuation and outlook: We have revised our NII estimates by -0.3%/-0.4%, PPOP estimates by -0.4%/-0.6% and PAT estimates by -0.6%/-5.7% for FY20/FY21, respectively. We upgrade RBL to Buy rating, revising our target price to Rs463 (from Rs559 earlier) and valuing the stock at 1.9x FY21E P/BV.

BUY

Sector: Banking

CMP: Rs364

Target Price: Rs463

Upside: 27%

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Key Data

Current Shares O/S (mn)	429.4
Mkt Cap (Rsbn/US\$bn)	155.3/2.2
52 Wk H / L (Rs)	717/360
Daily Vol. (3M NSE Avg.)	3,876,904

Price Performance (%)

	1 M	6 M	1 Yr
RBL Bank	(42.8)	(37.6)	(36.0)
Nifty Index	(8.1)	(1.9)	(4.7)

Source: Bloomberg

Exhibit 1: Change in our estimates

	Revised estimate		Earlier estimate		% Revision	
	FY20E	FY21E	FY20E	FY21E	FY20E	FY21E
Net interest income (Rsmn)	34,958	45,230	35,057	45,428	(0.3)	(0.4)
NIM (%)	4.16	4.27	4.17	4.29	-1 bps	-2 bps
Operating profit (Rsmn)	26,674	34,203	26,773	34,401	(0.4)	(0.6)
Profit after tax (Rsmn)	10,978	15,428	11,044	16,356	(0.6)	(5.7)

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 2: One-year forward P/BV



Source: Company, Nirmal Bang Institutional Equities Research

Financials

Exhibit 3: Income statement

Y/E March (Rsmn)	FY17	FY18	FY19	FY20E	FY21E
Interest income	37,132	45,076	63,007	82,459	104,849
Interest expenses	24,918	27,413	37,612	47,501	59,619
Net interest income	12,213	17,663	25,395	34,958	45,230
Fee income	4,912	7,226	11,656	15,301	19,719
Other income	2,642	3,456	2,768	3,479	4,367
Net revenues	19,768	28,345	39,818	53,739	69,316
Operating expenses	10,564	15,034	20,420	27,065	35,113
-Employee expenses	4,461	5,507	6,362	8,641	10,968
-Other expenses	6,102	9,527	14,058	18,424	24,145
Pre-provisioning Operating profit	9,204	13,311	19,398	26,674	34,203
Provisions	2,362	3,178	5,723	10,040	10,827
-Loan loss provision	1,975	2,995	5,234	9,394	10,054
-Investment depreciation	352	425	532	646	773
-Other provisions	35	(242)	(43)	0	0
PBT	6,842	10,133	13,676	16,633	23,376
Tax	2,382	3,782	5,006	5,655	7,948
PAT	4,460	6,351	8,670	10,978	15,428

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 5: Balance sheet

Y/E March (Rsmn)	FY17	FY18	FY19	FY20E	FY21E
Equity capital	3,752	4,197	4,267	4,480	4,480
Reserves & surplus	39,604	62,643	71,206	91,427	104,627
Shareholders' funds	43,356	66,840	75,473	95,908	109,108
Deposits	345,881	439,023	583,944	746,869	944,551
Borrowings	79,798	92,614	118,321	121,355	156,769
Other liabilities	17,713	20,031	25,850	39,936	55,919
Total liabilities	486,748	618,508	803,588	1,004,068	1,266,346
Cash/cash equivalent	41,936	42,844	66,021	52,951	67,777
Advances	294,490	402,678	543,082	706,007	903,689
Investments	134,817	154,475	168,404	218,185	267,063
Fixed assets	2,587	3,340	4,025	4,427	4,870
Other assets	12,917	15,170	22,056	22,497	22,947
Total assets	486,748	618,508	803,588	1,004,068	1,266,346

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 4: Key ratios

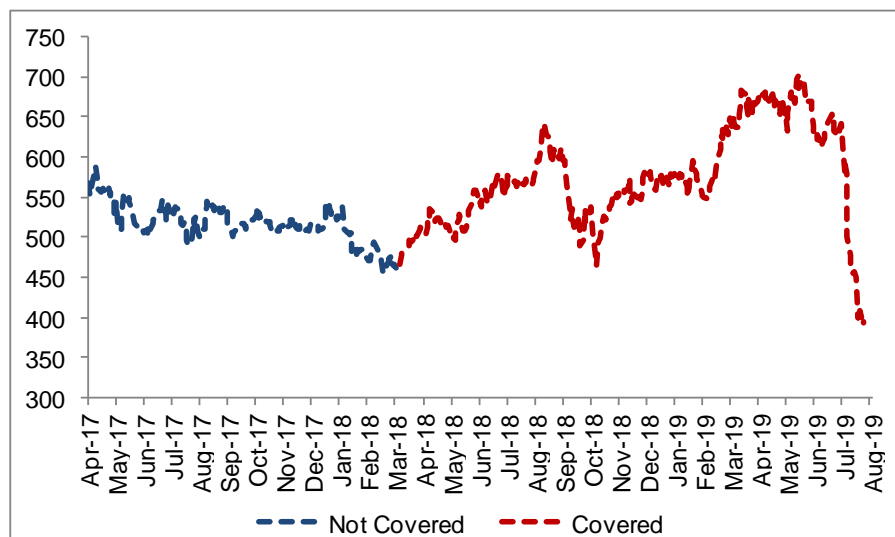
Y/E March	FY17	FY18	FY19	FY20E	FY21E
Growth (%)					
NII growth	49.1	44.6	43.8	37.7	29.4
Pre-provision profit growth	69.7	44.6	45.7	37.5	28.2
PAT growth	52.5	42.4	36.5	26.6	40.5
Business (%)					
Deposit growth	42.1	26.9	33.0	27.9	26.5
Advance growth	38.7	36.7	34.9	30.0	28.0
Business growth	40.5	31.4	33.9	28.9	27.2
CD	85.1	91.7	93.0	94.5	95.7
CASA	22.0	24.3	25.0	26.5	28.0
Operating efficiency (%)					
Cost-to-income	53.4	53.0	51.3	50.4	50.7
Cost-to-assets	2.4	2.7	2.9	3.0	3.1
Productivity (Rsmn)					
Business per branch	2679.4	3176.2	3478.5	3725.3	4107.2
Business per employee	130.6	158.8	192.9	201.4	222.0
Profit per branch	18.7	24.0	26.8	28.1	34.3
Profit per employee	0.9	1.2	1.5	1.5	1.9
Spreads (%)					
Yield on advances	10.4	9.8	10.7	10.8	10.8
Yield on investments	7.0	6.9	6.8	7.1	7.0
Cost of deposits	6.7	6.0	6.3	6.2	6.2
Yield on assets	9.0	8.8	9.5	9.8	9.9
Cost of funds	6.4	5.7	6.1	6.0	6.1
NIM	3.0	3.4	3.8	4.2	4.3
Capital adequacy (%)					
Tier I	11.4	13.6	12.1	11.0	9.8
Tier II	2.3	1.7	1.4	1.3	1.2
Total CAR	13.7	15.3	13.5	12.3	10.9
Asset quality (%)					
Gross NPAs	1.2	1.4	1.4	2.1	1.8
Net NPAs	0.6	0.8	0.7	0.6	0.1
Provision coverage	46.8	44.8	50.6	69.8	96.1
Slippage	2.1	1.6	1.5	2.2	1.8
Credit cost	0.6	0.7	1.0	1.4	1.2
Return (%)					
RoE	12.2	11.5	12.2	12.8	15.1
RoA	1.0	1.1	1.2	1.2	1.4
RoRWA	1.4	1.5	1.6	1.5	1.5
Per share (%)					
EPS	12.6	15.8	20.5	25.1	34.4
BV	115.6	159.3	176.9	214.1	243.5
ABV	110.5	151.8	168.1	204.1	242.1
Valuation (x)					
P/E	28.9	23.0	17.8	14.5	10.6
P/BV	3.1	2.3	2.1	1.7	1.5
P/ABV	3.3	2.4	2.2	1.8	1.5

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	463

Rating track graph



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BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

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