

July 30, 2022

**RESULT REPORT Q1 FY23** | Sector: Banks

# DCB Bank

## Margin decline and opex rise not comforting

### Result Highlights

- ✓ **Asset quality:** Gross slippages amounted to Rs 5.71bn (annualized slippage ratio of 7.9%) but recoveries and upgrades were also healthy at Rs 5.70bn
- ✓ **Margin picture:** NIM at 3.61% was down -32bps QoQ, sequentially lower due to excess liquidity that had to be maintained at the beginning of the quarter
- ✓ **Asset growth:** Advances grew 2.5%/16.9% QoQ/YoY driven sequentially by all segments except co-lending
- ✓ **Opex control:** Total opex rose 9.4%/31.9% QoQ/YoY, employee expenses rose 6.1%/26.4% QoQ/YoY and other expenses rose 13.2%/38.3% QoQ/YoY
- ✓ **Fee income:** Commission, exchange, brokerage fell/rose -2.3%/37.3% QoQ/YoY, significantly up YoY due to low base

### Our view - Margin decline and opex rise not comforting

**Excess liquidity was partly seasonal and partly due to meeting wholesale lending demand:** Management stated that the stable NIM would be in the range of 365-375 bps. 40 bps worth of repo rate hike has been passed on whereas, the remaining 50 bps hike will be passed on in August. The reset period for EBLR-linked loans is 3 months. Other than tractor loans, CV and gold loans, the loan book is essentially on floating rate.

**Management stated that the bank has been adding frontline staff and branches and opex would remain elevated this financial year:** New employees have been hired for various businesses across the board including mortgages, home loans, gold loans, tractors, CASA and term deposits, operations, credit and technology. In terms of medium-term guidance, in about 4-5 quarters, cost to income ratio would decline to 55%. Cost to average assets would come down as volume moves up.

**Elevated gross slippages for the quarter were driven by the gold loan book due to the 'Out of Order' circular of RBI but were essentially transient in nature:** In the gold loan book, the bank provides an OD product which requires monthly repayment whereas, some customers are used to bullet repayments (at the end of the tenure), which NBFCs used to offer them. Management guided that slippages from the mortgages, CV and SME book would be at or below the pre-Covid level in 2-3 quarters. Credit cost in the current financial year would be lower than in FY22 and on a steady state basis, would be 50-60 bps. The outstanding standard restructured advances stood at Rs 20.94 bn or 6.85% of gross advances but most of this book comprises secured loans.

**We downgrade DCB to 'Neutral' from 'Add' with an unchanged price target of Rs 95:** We value the bank at 0.6x FY24 P/BV for an FY23E/24E/25E RoE profile of 8.9/11.5/12.7%. The stock remains right at the bottom of our pecking order.

(See Comprehensive con call takeaways on page 2 for significant incremental colour.)

### Exhibit 1: Result table

(Rs mn)	Q1 FY23	Q4 FY22	% qoq	Q1 FY22	% yoy
Total Interest Income	9,493	9,199	3.2	8,455	12.3
Interest Expense	(5,753)	(5,395)	6.6	(5,368)	7.2
Net Interest Income	3,740	3,805	(1.7)	3,087	21.1
Other income	924	1,148	(19.5)	1,212	(23.7)
Total Income	4,664	4,953	(5.8)	4,299	8.5
Operating expenses	(3,002)	(2,744)	9.4	(2,277)	31.9
PPOP	1,661	2,208	(24.8)	2,022	(17.8)
Provisions	(350)	(676)	(48.2)	(1,565)	(77.6)
PBT	1,311	1,532	(14.4)	457	187.2
Tax	(340)	(398)	(14.6)	(119)	185.7
PAT	971	1,134	(14.4)	338	187.8

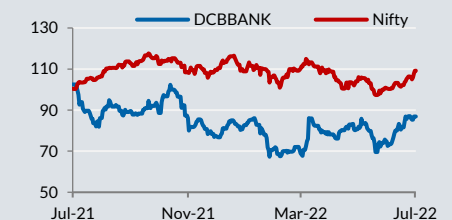
Source: Company, YES Sec-Research

Recommendation	: <b>NEUTRAL</b>
Current Price	: Rs 89
Target Price	: Rs 95
Potential Return	: 6%

### Stock data (as on July 29, 2022)

Nifty	17,158
52 Week h/l (Rs)	106 / 68
Market cap (Rs/USD mn)	27713 / 350
Outstanding Shares (mn)	311
6m Avg t/o (Rs mn):	98
Div yield (%):	1.1
Bloomberg code:	DCBB IN
NSE code:	DCBBANK

### Stock performance



	1M	3M	1Y
Absolute return	18.6%	12.7%	-14.1%

### Shareholding pattern (As of Jun'22 end)

Promoter	14.9%
FII+DII	50.1%
Others	35.1%

### Δ in stance

(1-Yr)	New	Old
Rating	NEUTRAL	ADD
Target Price	95	95

### Financial Summary

(Rs mn)	FY23E	FY24E	FY25E
NII	15,812	18,220	21,223
PPOP	8,771	10,717	12,945
Net Profit	3,741	5,301	6,556
Growth (%)	30.1	41.7	23.7
EPS (Rs)	12.0	17.0	21.1
BVPS (Rs)	141	157	176
P/E (x)	7.4	5.2	4.2
P/BV (x)	0.6	0.6	0.5
ROE (%)	8.9	11.5	12.7
ROA (%)	0.8	1.0	1.0
Tier-1 (%)	14.7	13.5	12.6

### Δ in earnings estimates

Rs.	FY23E	FY24E	FY25E
EPS (New)	12.0	17.0	21.1
EPS (Old)	13.2	17.2	21.1
% change	-9.0%	-1.2%	0.1%

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## COMPREHENSIVE CON-CALL TAKEAWAYS

### Asset quality

#### ✓ Slippages and NPA movement

##### • Slippages

- Gross NPA additions amounted to Rs 5.71bn for 1QFY23, translating to an annualized slippage ratio of 7.9% for the quarter. (Gross NPA additions had amounted to Rs 3.80bn during 4QFY22.)
- **Segmental colour**
  - Slippages were driven by the gold loan book.
  - The slippages from the CV and mortgages book were back to close to pre-Covid levels.
  - There were some slippages from the AIB book driven by KCC, where the recovery is generally good.
- **Out of order Circular**
  - As such, slippages were driven by the RBI November 2021 Circular, which states that if an account has not serviced its interest even on a single day for the past 90 days, it would be regarded as out of order and tagged a slippage.
  - In the gold loan book, the bank provides an OD product which requires monthly repayment whereas, some customers are used to bullet repayments (at the end of the tenure), which NBFCs used to offer them.
- **Slippage guidance**
  - Slippages from the mortgages, CV and SME book would be at or below the pre-Covid level in 2-3 quarters.

##### • Recoveries and upgrades

- Recoveries and upgrades amounted to Rs 5.70bn for 1QFY23, implying net NPA addition of almost nil for the quarter.
- Upgrades were much higher than recoveries.
- Upgrades were also driven by the gold loan book.
- There are 900 in-house employees focused on recovery.

#### ✓ Provisions

- Provisions were Rs 350mn, down by -48.2% QoQ and -77.6% YoY.
- **Credit cost guidance**
  - Credit cost in the current financial year would be lower than in FY22.
  - On a steady state basis, credit cost would be 50-60 bps.
  - In terms of when steady state would be achieved, management stated that the bank expects to reach normal pre-Covid level of slippages in 2-3 quarters.
- **Provision coverage**
  - Provision coverage ratio is 69.5%.
  - Excluding the gold loan book, the provision coverage ratio is 72%.
  - The bank makes 15% provision on gold loan NPA as per norms but, longer term, the coverage required on gold loan NPA is lesser.

#### ✓ Restructured book

- The outstanding standard restructured advances stood at Rs 20.94 bn or 6.85% of gross advances.
- Restructured book is holding up well.
- Most of the restructured book is secured.
- The restructured book has declined by Rs 0.6bn on sequential basis (on gross basis).

(Con call takeaways continue on the next page)

**✓ ECLGS book**

- The disbursement has been Rs 10bn from a sanction of Rs 20-30bn.
- There have some slippages and some upgrades.

**✓ Granularity**

- The overall loan book remains granular with 84% of loan book having a ticket size of less than Rs 30mn.
- The top 5 borrowers are less than 5% of loan book.

**Liabilities traction**

- ✓ CASA deposits have grown at 51% YoY. (Overall deposits growth was 14.6% YoY).
- ✓ Within this, SA deposits grew more than 60% YoY, driven by branch banking.

**Loan growth****✓ Loan growth for the quarter**

- Level of disbursement was similar to level in 4QFY22.
- Loan growth was somewhat slow in the first quarter due repayments on gold loan book and low SME utilisation levels.

**✓ Co-lending**

- Disbursement in co-lending declined due to limits set.
- The bank is looking for new co-lending partners.
- In the future, co-lending could contribute about 5% to loan book.

**✓ Share of mortgages**

- Share of mortgages including the mortgages portion of AIB and others is 47-48%.
- This could rise to 50-55% going forward.

**✓ Loan growth guidance**

- Management was confident of growth from mortgages, tractors, KCC, gold loans and new co-lending sign-ups.
- The bank is not particularly concerned about bank competition as the average ticket size for mortgages is Rs 3-4mn, a segment which the bank understands quite well.
- Management believes that it can double the balance sheet in about 3-4 years.
- In the recent years, growth had been slow since the bank had taken a defensive stance in 2020 and 2021.

**Operating expenses****✓ Near term opex**

- The bank has been adding frontline staff and branches and opex would be elevated in this financial year.
- New employees have been hired for various businesses across the board including mortgages, home loans, gold loans, tractors, CASA and term deposits, operations, credit and technology.

**✓ Medium-term guidance**

- In about 4-5 quarters, cost to income ratio would decline to 55%.
- Cost to average assets would come down as volume moves up.

(Con call takeaways continue on the next page)

## Fee income

- ✓ Core fee income is doing well and was Rs 648mn during the quarter compared with Rs 663mn in 4QFY22.

## Treasury income

- ✓ There was no treasury loss but rather a treasury gain of about Rs 50-60mn for the quarter.
- ✓ Last year, the treasury gain in the first quarter had been more than Rs 0.5bn.

## Net interest margin

- ✓ **NIM for the quarter**
  - NIM declined 32 bps QoQ to 3.61%.
  - NIM was dragged lower, among other factors, due to excess liquidity that had to be maintained at the beginning of the quarter.
  - Excess liquidity was partly seasonal and partly due to meeting wholesale lending demand.
- ✓ **NIM guidance**
  - The stable NIM would be in the range of 365-375 bps.
- ✓ **Floating rate loans**
  - **Transmission in EBLR-linked loans**
    - 40 bps worth of repo rate hike has been passed on.
    - The remaining 50 bps hike will be passed on in August.
    - The reset period is 3 months.
  - **Share of floating rate loans**
    - Other than tractors, CV and gold loans, the loans are on floating rate.
- ✓ **Cost of deposits**
  - The cost of deposits has come down on sequential basis.
  - Management stated that they have to be competitive on rates.
- ✓ **Refinancing**
  - The bank benefits since its portfolio can be refinanced by entities like NABARD.
- ✓ **Priority sector lending**
  - About 60% of the book is PSL-compliant.

## Exhibit 2: Key quarterly balance sheet / business data

(Rs mn)	Q1 FY23	Q4 FY22	% qoq	Q1 FY22	% yoy
Advances	298,140	290,958	2.5	254,956	16.9
Corporate banking	29,814	29,096	2.5	28,045	6.3
AIB	62,609	61,101	2.5	56,090	11.6
CV	8,944	8,729	2.5	12,748	(29.8)
Gold Loans	14,907	14,548	2.5	15,297	(2.6)
Mortgage	125,219	119,293	5.0	109,631	14.2
SME and MSME	26,833	26,186	2.5	25,496	5.2
Co-Lending	17,888	20,367	(12.2)	2,550	601.6
Other Loans	11,926	11,638	2.5	5,099	133.9
Total Deposits	350,810	346,917	1.1	306,017	14.6
CASA	100,240	92,811	8.0	66,387	51.0
Term	250,570	254,106	(1.4)	239,630	4.6
RWA	249,380	243,128	2.6	231,066	7.9

Source: Company, YES Sec – Research

## Exhibit 3: Key quarterly ratios

(%)	Q1 FY23	Q4 FY22	chg qoq	Q1 FY22	chg yoy
Net interest margin	3.61	3.93	-32bps	3.31	30bps
Yield on advances	10.65	11.00	-35bps	10.50	15bps
Cost of funds	6.00	6.04	-4bps	6.34	-34bps
Loan to Deposit ratio	85.0	83.9	111bps	82.6	234bps
Non-interest income/Total income	19.8	23.2	-336bps	28.2	-837bps
Cost to Income	64.4	55.4	897bps	53.0	1141bps
RoE	10.1	12.1	-200bps	3.8	633bps
RoA	0.9	1.1	-20bps	0.3	52bps
Annualised Slippage Ratio	7.9	5.6	226bps	8.1	-22bps
Provision Coverage	69.5	67.8	164bps	59.4	1006bps
Gross NPA	4.2	4.3	-11bps	4.9	-66bps
Net NPA	1.8	2.0	-15bps	2.8	-100bps
Capital adequacy ratio	18.5	18.9	-45bps	19.6	-117bps
Tier I capital ratio	15.4	15.8	-40bps	15.5	-10bps

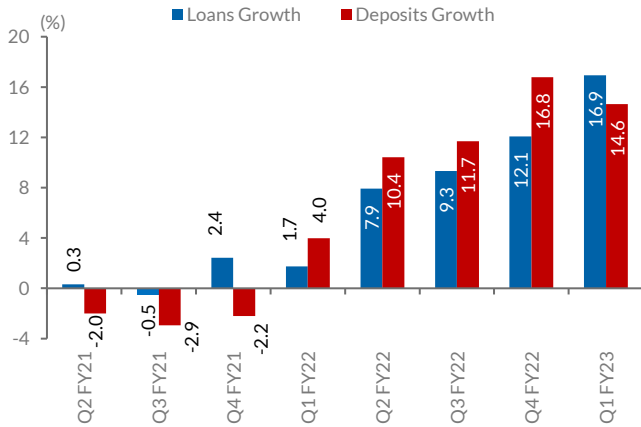
Source: Company, YES Sec – Research

## Exhibit 4: Quarterly Actuals Vs Estimates

Q1FY23 (Rs. mn)	Actuals	Estimates	Diff, %
Net Interest Income	3,740	3,946	(5.2)
Pre-Prov. Operating Profit	1,661	1,850	(10.2)
Profit After Tax	971	823	18.1

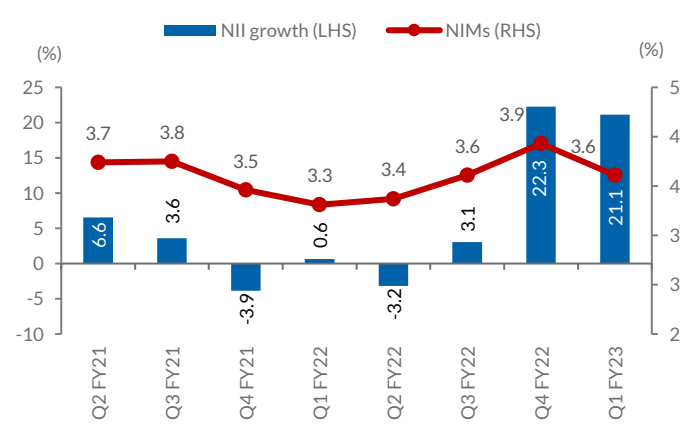
Source: Company, YES Sec – Research

**Exhibit 5: Loans and Deposits growth (YoY %)**



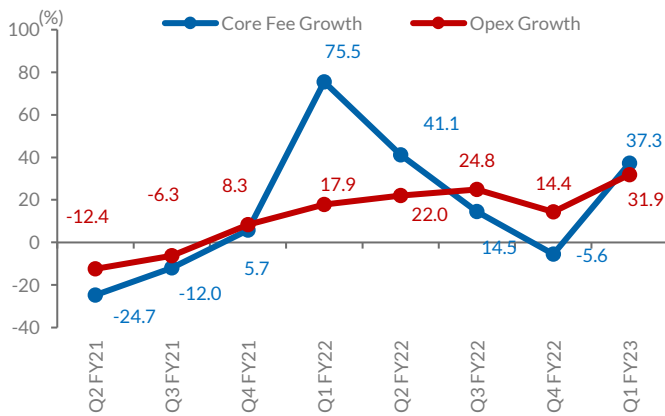
Source: Company, YES Sec – Research

**Exhibit 6: NII growth (YoY %) and NIM**



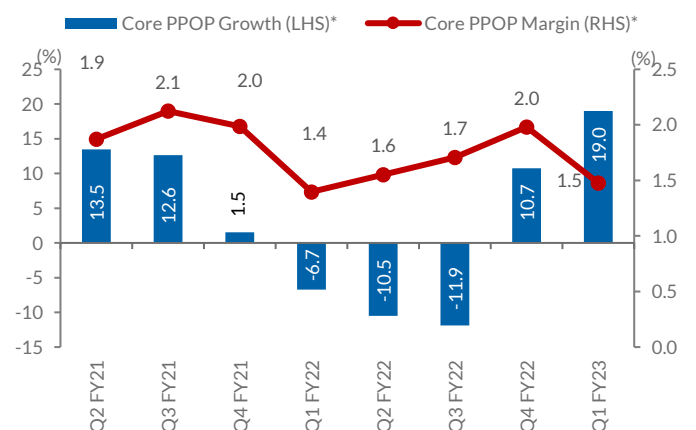
Source: Company, YES Sec – Research

**Exhibit 7: Core Fee and Opex growth (YoY %)**



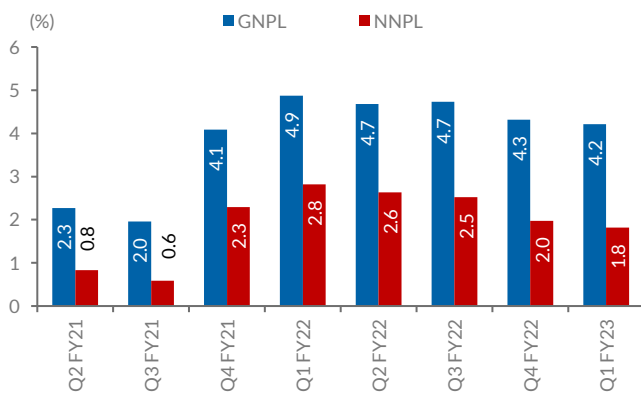
Source: Company, YES Sec – Research

**Exhibit 8: Core PPOP growth (YoY %) and Core PPOP margin**



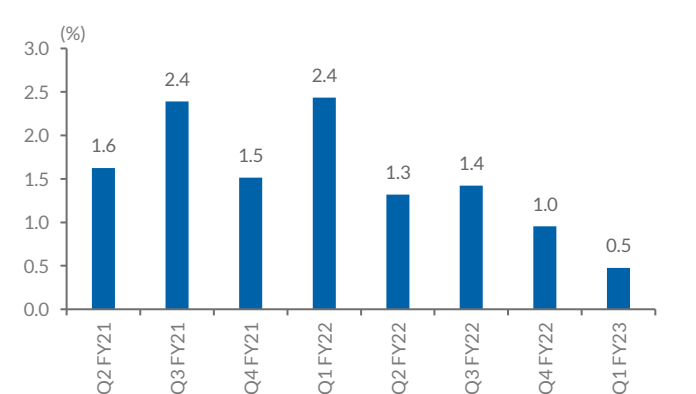
Source: Company, YES Sec – Research, \* Core PPOP is derived by adjusting PPOP for gain/loss on sale of investments and misc. income

**Exhibit 9: Gross NPA and Net NPA (%)**



Source: Company, YES Sec – Research

**Exhibit 10: Provisions/Average Advances (%)**



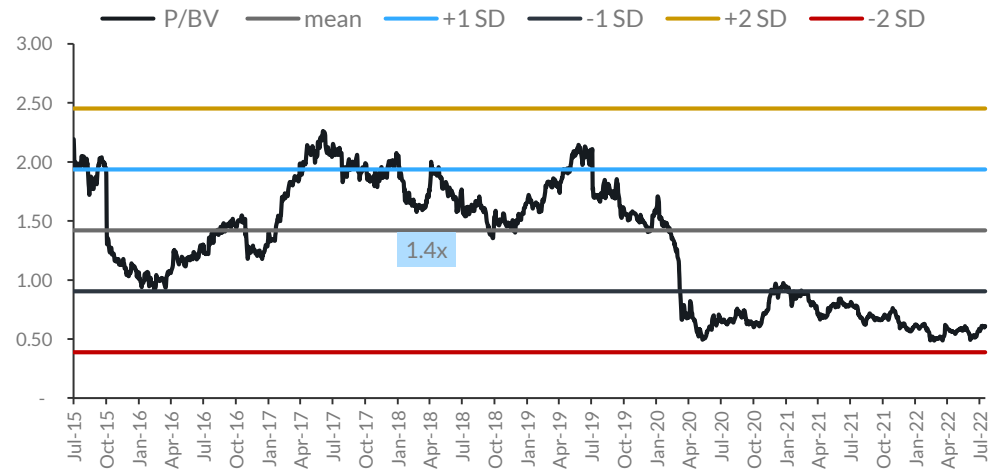
Source: Company, YES Sec – Research

**Exhibit 11: 1-year rolling P/BV band**



Source: Company, YES Sec - Research

**Exhibit 12: 1-yr rolling P/BV vis-a-vis the mean and standard deviations**



Source: Company, YES Sec - Research

## ANNUAL FINANCIALS

### Exhibit 13: Balance sheet

Y/e 31 Mar (Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
Total cash & equivalents	30,393	40,908	40,152	46,175	53,101
Investments	84,137	90,982	105,020	120,996	139,288
Advances	259,592	290,958	334,601	384,792	442,510
Fixed assets	5,685	6,612	7,273	8,000	8,800
Other assets	16,213	18,942	28,413	28,981	29,561
<b>Total assets</b>	<b>396,021</b>	<b>448,401</b>	<b>515,460</b>	<b>588,944</b>	<b>673,260</b>
Net worth	37,586	40,488	43,874	48,672	54,605
Deposits	297,039	346,917	403,654	468,901	543,935
Borrowings	44,823	40,818	45,129	46,489	47,928
Other liabilities	16,574	20,178	22,803	24,883	26,792
<b>Total liabilities incl. Equity</b>	<b>396,021</b>	<b>448,401</b>	<b>515,460</b>	<b>588,944</b>	<b>673,260</b>

Source: Company, YES Sec – Research

### Exhibit 14: Income statement

Y/e 31 Mar (Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
Interest income	34,582	35,128	40,896	47,391	55,031
Interest expense	(21,716)	(21,553)	(25,084)	(29,171)	(33,808)
<b>Net interest income</b>	<b>12,866</b>	<b>13,575</b>	<b>15,812</b>	<b>18,220</b>	<b>21,223</b>
Non-interest income	4,585	4,520	4,637	5,631	6,479
<b>Total income</b>	<b>17,451</b>	<b>18,095</b>	<b>20,449</b>	<b>23,851</b>	<b>27,702</b>
Operating expenses	(8,466)	(10,126)	(11,678)	(13,135)	(14,757)
<b>PPoP</b>	<b>8,985</b>	<b>7,970</b>	<b>8,771</b>	<b>10,717</b>	<b>12,945</b>
Provisions	(4,457)	(4,074)	(3,715)	(3,553)	(4,086)
<b>Profit before tax</b>	<b>4,528</b>	<b>3,895</b>	<b>5,056</b>	<b>7,164</b>	<b>8,860</b>
Taxes	(1,170)	(1,020)	(1,314)	(1,863)	(2,304)
<b>Net profit</b>	<b>3,358</b>	<b>2,875</b>	<b>3,741</b>	<b>5,301</b>	<b>6,556</b>

Source: Company, YES Sec – Research



## Exhibit 15: Du Pont Analysis (RoA tree)

Y/e 31 Mar (Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
Interest income	8.9	8.3	8.5	8.6	8.7
Interest expense	-5.6	-5.1	-5.2	-5.3	-5.4
<b>Net interest income</b>	<b>3.3</b>	<b>3.2</b>	<b>3.3</b>	<b>3.3</b>	<b>3.4</b>
Non-interest income	1.2	1.1	1.0	1.0	1.0
<b>Total income</b>	<b>4.5</b>	<b>4.3</b>	<b>4.2</b>	<b>4.3</b>	<b>4.4</b>
Operating expenses	-2.2	-2.4	-2.4	-2.4	-2.3
<b>PPoP</b>	<b>2.3</b>	<b>1.9</b>	1.8	1.9	2.1
Provisions	-1.1	-1.0	-0.8	-0.6	-0.6
<b>Profit before tax</b>	<b>1.2</b>	<b>0.9</b>	<b>1.0</b>	<b>1.3</b>	<b>1.4</b>
Taxes	-0.3	-0.2	-0.3	-0.3	-0.4
<b>Net profit</b>	<b>0.9</b>	<b>0.7</b>	<b>0.8</b>	<b>1.0</b>	<b>1.0</b>

Source: Company, YES Sec – Research

## Exhibit 16: Change in annual estimates

Y/e 31 Mar (Rs mn)	Revised Estimate			Earlier Estimate			% Revision		
	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
Net Interest Income	15,812	18,220	21,223	15,831	18,228	21,133	(0.1)	(0.0)	0.4
Pre-Prov. Operating Profit	8,771	10,717	12,945	9,270	10,800	12,938	(5.4)	(0.8)	0.1
Profit after tax	3,741	5,301	6,556	4,111	5,363	6,551	(9.0)	(1.2)	0.1

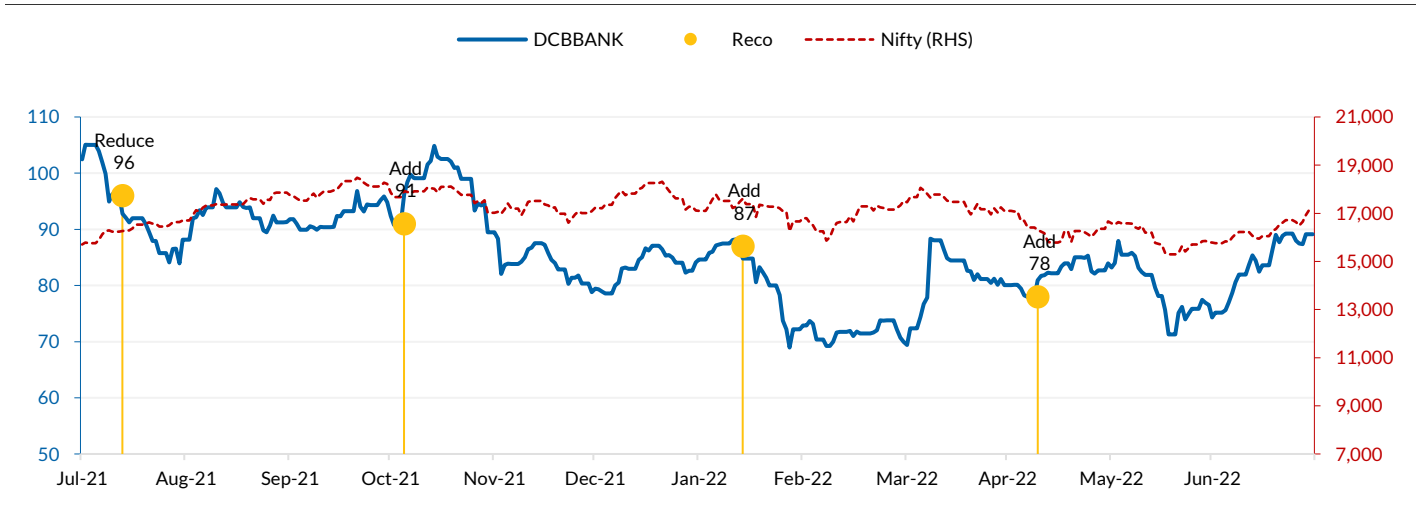
Source: Company, YES Sec – Research

## Exhibit 17: Ratio analysis

Y/e 31 Mar	FY21	FY22	FY23E	FY24E	FY25E
<b>Growth matrix (%)</b>					
Net interest income	1.7	5.5	16.5	15.2	16.5
PPoP	19.3	-11.3	10.1	22.2	20.8
Net profit	-0.6	-14.4	30.1	41.7	23.7
Loans	2.4	12.1	15.0	15.0	15.0
Deposits	-2.2	16.8	16.4	16.2	16.0
<b>Profitability Ratios (%)</b>					
Net interest margin	3.6	3.6	3.7	3.7	3.8
Return on Average Equity	9.4	7.4	8.9	11.5	12.7
Return on Average Assets	0.9	0.7	0.8	1.0	1.0
<b>Per share figures (Rs)</b>					
EPS	10.8	9.2	12.0	17.0	21.1
BVPS	121	130	141	157	176
ABVPS	102	112	114	135	159
<b>Valuation multiples</b>					
P/E	8	10	7.4	5.2	4.2
P/BV	0.7	0.7	0.6	0.6	0.5
P/ABV	0.9	0.8	0.8	0.7	0.6
<b>NIM internals (%)</b>					
Yield on loans	10.9	10.3	10.6	10.7	10.8
Cost of deposits	6.3	5.9	5.8	5.9	6.0
Loan-deposit ratio	87.4	83.9	82.9	82.1	81.4
CASA ratio	22.8	26.8	28.5	29.0	29.5
<b>Opex control (%)</b>					
Cost/Income ratio	48.5	56.0	57.1	55.1	53.3
Cost to average assets	2.2	2.4	2.4	2.4	2.3
<b>Capital adequacy (%)</b>					
Tier 1 capital ratio	15.5	15.8	14.7	13.5	12.6
<b>Asset quality (%)</b>					
Slippage ratio	2.7	6.4	4.5	2.5	2.0
Gross NPL ratio	4.1	4.3	4.3	2.9	2.1
Credit cost	1.0	1.0	1.2	1.0	1.0
Net NPL ratio	2.3	2.0	2.5	1.7	1.2

Source: Company, YES Sec – Research

## Recommendation Tracker



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