

Stock Note

Union Bank of India

September 15, 2023





Industry	LTP	Recommendation	Base Case Fair Value	Bull Case Fair Value	Time Horizon
PSU Banks	Rs. 94.5	Buy between Rs. 93.5 – 95.5 & add more on dips to Rs. 80-82 band	Rs. 105	Rs. 116	2-3 quarters

HDFC Scrip Code	UNIBANEQNR
BSE Code	532477
NSE Code	UNIONBANK
Bloomberg	UNBK:IN
CMP September 14, 2023	94.5
Equity Capital (Rs Cr)	6835
Face Value (Rs)	10
Equity Share O/S (Cr)	683.5
Market Cap (Rs Cr)	70040
Adjusted Book Value (Rs) (FY23)	83.6
Avg. 52 Wk Volumes	19109057
52 Week High	96.8
52 Week Low	41.9

Share holding Pattern % (June, 2023)	
Promoters	83.5
Institutions	9.7
Non Institutions	6.8
Total	100.0



HDFCsec Retail research
stock rating meter

for details about the ratings, refer at the end of the report

* Refer at the end for explanation on Risk Ratings

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Our Take:

Union Bank of India has seen strong improvement in the performance in last couple of quarters - Coverage on impaired loans has risen, capitalization level has reached healthy levels and has also approved a fund raise (QIP of Rs.5000 crores), lower fresh NPA and higher focus on CASA ratio etc. We feel that there is still room for the upside even as the credit growth in the banking sector is continuing. Further, underwriting practices have improved as observed from the rising share of the retail segment and incremental corporate lending done to better rated corporates. Lower slippages along with healthy rate of recoveries are helping the bank reduce credit cost which ultimately results in increased RoA.

Post the amalgamation with Andhra Bank and Corporation Bank, Union Bank of India (UBI) has become fifth largest public sector bank in terms of total business. With over a century of banking operations in India, it has become an established player. Apart from banking, it also has presence across various financial services via Subsidiaries and JVs. The bank has well-balanced asset mix and it has started focusing on Retail, Agriculture and MSME (“RAM”) sectors which will lead to better risk diversification, increased revenues and improved margins. In recent times, the bank has done significant investment for digitization and has done tie ups with Fintechs, which is expected to improve margins and bring incremental sales in the coming quarters. The bank has also developed significant sources of fee based income which is granular by nature.

Valuation & Recommendation:

UBI has reported healthy YoY performance in Q1FY24, supported by strong traction in loan book and improvement in asset quality. The management has guided for 10-12% growth in loan book for FY24. Further, GNPA and NNPA are expected to be less than 6% and 1% respectively. We have envisaged 10% CAGR in NII and 22% CAGR in net profit over FY23-25E while loan book is expected to grow by 11% CAGR over same time frame. ROAA is estimated to improve to 0.85% by the end of FY25E. It is still trading at inexpensive valuation of 0.8x FY25E P/ABV. We are not separately ascribing any value to the subsidiaries/associates of UBI while valuing the stock.

We feel investors can buy the shares of Union Bank of India between Rs. 93.5 – 95.5 (0.8x FY25E ABV) & add more on dips of Rs. 80-82 (0.7x FY25E ABV) for the base case fair value of Rs. 105 (0.9x FY25E ABV) and for the bull case fair value of Rs. 116 (1.0x FY25E ABV) over the next 2-3 quarters.



Financial Summary

	Q1FY24	Q1FY23	YoY (%)	Q4FY23	QoQ (%)	FY21	FY22	FY23	FY24E	FY25E
NII	8840	7582	17	8251	7	24688	27786	32765	35493	39718
PPP	7179	5448	32	6823	5	19667	21873	25467	26406	30487
PAT	3236	1558	108	2782	16	2906	5232	8433	9941	12592
EPS (Rs)						4.5	7.7	12.3	14.5	18.4
ABV						45.1	55.6	83.6	101.2	116.1
P/E (x)						20.8	12.3	7.7	6.5	5.1
P/ABV (x)						2.1	1.7	1.1	0.9	0.8
RoAA (%)						0.4	0.5	0.7	0.7	0.8
RoAE (%)						5.9	7.7	11.3	12.1	13.8

(Source: Company, HDFC sec)

Recent Developments

Q1FY24 Result Update

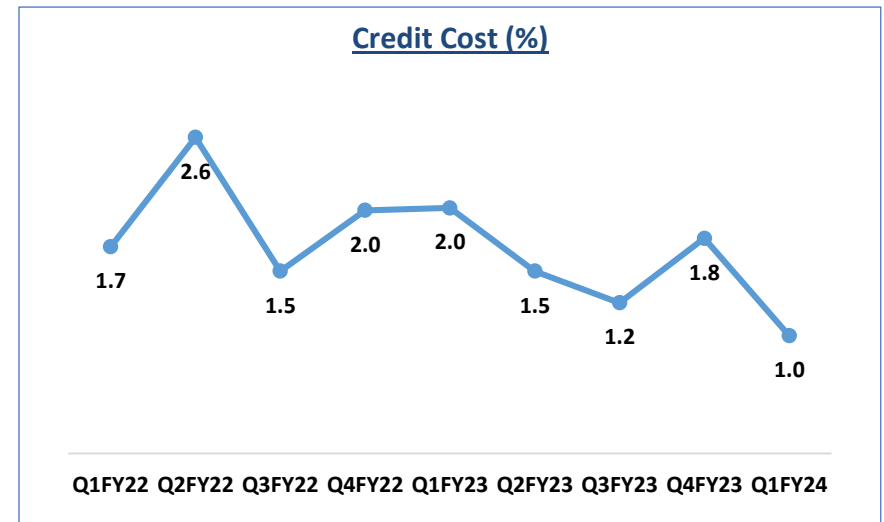
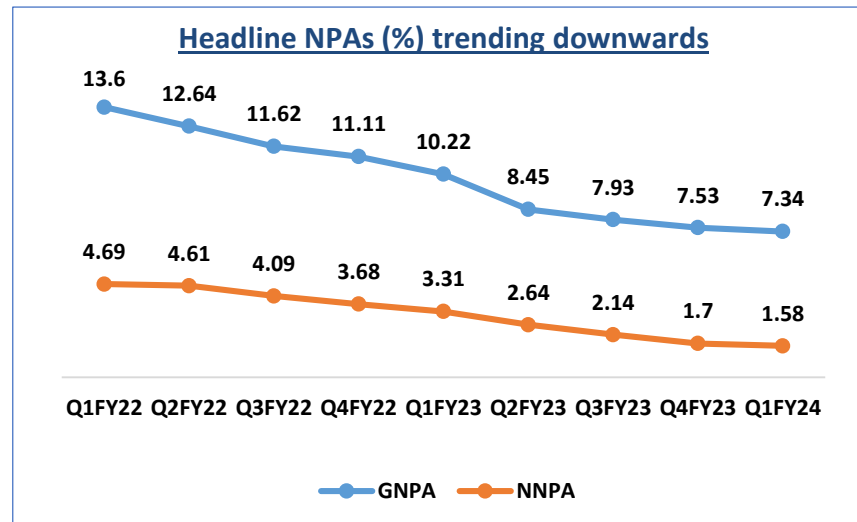
The bank reported Net Interest Income of Rs. 8,840 crores, up 17/7% YoY/QoQ. This increase in its NII was backed by its Net Interest Margins (NIM), which stood at 3.13% for Q1FY24 as against 2.98% in Q4FY23 and 3% in Q1FY23, driven by robust growth in Yield on advances of 129/40bps YoY/QoQ, at 8.43%. Further, the bank reported a total of Rs. 3,903 crores under other income, which is up 39% YoY. However, this includes some one time incomes which are not expected to recur in the coming quarters, such as interest on income tax refund of ~Rs. 300 crores, income from sale of PSLCs at Rs. 550 crores and inflated recoveries on written off loans of Rs. 690 crores. The Cost of Deposits stood at 4.97%, up 94/16bps YoY/QoQ. It reported a 39% YoY increase in its other income and was able to control its cost to income ratio, which stood at 43.66% for the quarter, as against 49.53% in Q4FY23 and 47.61% in Q1FY23. Its total opex were lower 17% on a sequential basis, driven by lower sequential employee expenses (23%) as Q4FY23 had one-time family pension expenses, and lower other expenses (7%) on account of cyclicity. Its PPOP stood at Rs. 7,179 crores, up 32/5% YoY/QoQ. The credit costs for Q1FY24 stood at 0.97%, which is better compared to 1.77% in Q4FY23 and 2.02% in Q1FY23. The reported profit after tax of Rs. 3,236 crores, up 108/16% YoY/QoQ.

In terms of financial position, it reported total deposits worth Rs. 11,28,052 crores, up 14/1% YoY/QoQ. Its CASA ratio stood at 34.6% as of June 2023, declining from 35.62% in March 2023 and 36.2% in June 2022. On the assets side, it reported total gross advances worth Rs. 8,18,457 crores, up 12/1% YoY/QoQ. The GNPA ratio stood at 7.34% for Q1FY24, down 288/19 bps YoY/QoQ, while the NNPA ratio stood at 1.58%, down 173/12 bps YoY/QoQ. Total Capital Adequacy Ratio stood at 15.95% with RoA at 1% and RoE at 18.97%. The Board has approved a plan to raise Rs. 10,100 crores including Rs.5000 crores by way of a QIP.



Improvement in asset quality

The bank has continued to report healthy improvement in its asset quality. Though the fresh slippages have increased to Rs. 3,032 crores, strong cash recoveries, upgrades and write offs helped the bank in improving its asset quality ratios. As of Q1FY24, the Gross NPA stood at 7.34% (down 288/19 bps YoY/QoQ) and Net NPA stood at 1.58% (down 173/12bps YoY/QoQ). Provision Coverage Ratio improved further by 52 bps sequentially at 90.86%. Credit cost for the quarter was at 0.97%, down from 2.02% in Q1FY23 and 1.77% in Q4FY23. The restructured book declined marginally to 2.6% of the total loans vs 2.9% in Q1FY23. The SMA book was mildly down 2bps from 53bps in Q1FY23 to 51bps in Q1FY24. Within its loan book, MSME and retail segment has contributed the most to the GNPA- 12.12% and 9.92% respectively, down from 17.62% and 11.85% as of Q1FY23.



(Source: Company, HDFC sec)

Concall Highlights:

- 90% of the total loan book consists of floating rate loans, within which 49% are MCLR linked and 41% are EBLR linked. 25% of the MCLR linked book of the bank has been repriced in the current quarter and ~Rs. 2.76 lakh crores worth of loans are expected to be repriced in the coming quarters.
- The bank has a target to achieve 50% of its RAM book disbursed and garner Rs. 1 trillion CASA via digital means.
- The bank is interested in tying up with ONDC going forward along with other Fintechs.
- The management has set a target of 1% annual RoA by the end of FY25.



- It expects its non-interest income to grow by 30% going forward.
- The bank has successfully settled 3 accounts worth Rs. 990 crores with 46% recoveries in the NARCL and more 20-25 accounts are in the process to fetch bids.
- The bank has not created any floating provisions for ECL as of Q1FY24 and it feels that its SMA2 book warrants more provisions. It is taking active steps to control this book. It does not expect the transition to ECL provisioning to have a material effect on its profitability.
- It has sanctioned ECLGS loans of ~Rs. 16,700 crores and has disbursed ~Rs. 8,700 crores with a GNPA of 5.93% of the sanctioned amount.
- The sequential reduction in employee cost was primarily on account of provision of family pension in Q4FY23 worth ~Rs. 1,500 crores.
- The bank expects corporate book growth to pick up in the coming quarter backed by healthy sanctions ready for disbursements.
- In terms of fee based income, the bank has set a target to tap the potential credit cards market.
- The management expects an increase in its cost of deposits as 27% of the total deposits are bulk deposits which are costlier than retail deposits by 20-30bps. Going ahead, it does not plan to accept bulk deposits.
- The target cost to income ratio is set to 45-50%. This target is backed by the potential benefits expected from the digitization drive in the bank, by the outsourcing of marketing and back office operations to UBI Services Ltd and by branch rationalization. On the income side, the bank wants to support the target set for cost to income ratio by focusing on fee based income from transaction banking, like wealth management, selling insurance products, etc.
- The management feels that going forward it does not require aggressive provisioning as it has done it in the past. Further, it is confident on its recovery mechanism and hence does not expect any substantial credit costs beyond a range of 1-15bps from the current levels.

Guidance for FY24

	Actual as of June 30, 2023	Guidance for FY24
Deposits Growth (YoY)	13.63%	8-10%
Advances Growth (YoY)	12.33%	10-12%
NIM (%)	3.13%	3.00%
Gross NPA (%)	7.34%	<6%
Net NPA (%)	1.58%	<1%
Slippages (Rs. in crores)	3,241	12,000
Recoveries (Rs. in crores)	3,564	16,000

(Source: Company, HDFC sec)



Key Triggers:

Established player

UBI is one of the oldest and largest public sector banks (PSBs) in India. Post amalgamation with Andhra Bank and Corporation Bank with itself effective from April 1, 2020, the size of the balance sheet had almost doubled, thereby increasing the bank's market share. The bank has emerged as the 5th largest in terms of total business. The bank has diversified presence across India with 8,561 branches and 10,195 ATMs and has 75,300+ employees. It also has overseas presence via 3 branches at Hong Kong, Dubai and Sydney. Furthermore, apart from banking, UBI also has presence in asset management, broking as well as life insurance businesses via its subsidiaries and Joint ventures. These association helps the bank in diversifying the business as well as it can raise capital via stake sale. Over the years, the bank has built a strong base of distributed clientele that has provided low cost funding and has been a source of strength for the liability portfolio.

Improved loan book quality

As of Q1FY24, the global advances stood at Rs.8,18,457 crores, of which ~97% are domestic advances. During Q1FY24, UBI has reported advance growth of 12/1% YoY/QoQ. Within this, domestic advances grew by 12/1% YoY/QoQ and overseas advances grew by 34/2% YoY/QoQ. The contribution from corporate advances was 46%, followed by retail at 20%, agriculture at 19% and MSME at 16% of the domestic advances as on 30th June, 2023. On a sequential basis, the bank has seen flat growth in the four broad loan segments, however, on a yearly basis, it saw good traction in RAM book of 16%, 13% and 15% respectively. Within the retail book, the bank saw a yearly increase of 65% in personal loans, 33% in educational loans and 29% in vehicle loans. In the concall, the management specified that they are focusing more on high yielding educational loans, to aspirants of premier universities/ institutes abroad which indirectly reduces the risk component associated with such loans as well. On the corporate side, the growth has been almost flat on a sequential basis but the management in the concall specified that it has sanctioned a total of Rs. 25,000 crores of corporate loans which are expected to be disbursed in the current FY-24 and hence, going forward, the corporate book is also expected to catch pace.

The quality of the loan book has also improved a lot lately, on the corporate book side, the BB and below rated book stands at just 8% and 98% of the NBFC loans have been rated A and above. Further, 97% of retail loans have credit scores of 700 and above. Almost half of its retail book consists of housing loans. Gold loans and educational loans have performed the best in terms of YoY growth- 53% and 33% respectively. In its corporate book, the highest exposure was seen towards infrastructure, NBFCs and Housing Finance companies.

Management has given double digit (10-12%) loan book growth guidance for FY24.



	Q1FY24	Q4FY23	Q1FY23	YoY	QoQ	Mix (%)
Domestic	7,93,448	7,85,302	7,09,904	12%	1%	97%
Overseas	25,009	24,603	18,731	34%	2%	3%
Gross Advances	8,18,457	8,09,905	7,28,635	12%	1%	
Corporate	3,74,724	3,73,188	3,42,527	9%	0%	46%
Retail	1,62,373	1,59,702	1,39,410	16%	2%	20%
Home Loan	80,537	79,372	72,704	11%	1%	10%
Vehicle Loan	16,887	16,449	13,135	29%	3%	2%
Education Loan	9,829	9,263	7,373	33%	6%	1%
Mortgage Loan	14,289	14,213	12,547	14%	1%	2%
Personal Loans	11,528	11,658	6,971	65%	-1%	1%
Others	29,303	28,746	26,681	10%	2%	4%
Agricultural	1,53,615	1,51,993	1,35,503	13%	1%	19%
MSME	1,27,745	1,25,022	1,11,195	15%	2%	16%

(Source: Company, HDFC sec)

Stable Liability Profile:

As of June 2023, the bank has garnered a total of Rs. 11,28,052 crores worth of deposits, which is up 14/1% YoY/QoQ. This consists of Rs. 11,12,887 crores domestic deposits, which have grown 12/1% YoY/QoQ. Within this, the CASA balances stood at Rs. 3,85,084 crores, up 7% YoY. Its CASA ratio stood at 34.6% as of June 2023, declining from 35.62% in March 2023 and 36.2% in June 2022. The CASA and Retail Term Deposits together make up 73% of the total deposits profile of the bank, rest being bulky wholesale term deposits. The bank has a comfortable Liquidity Coverage Ratio (LCR) of 161% and hence it feels it has sufficient liquidity going forward. The bank has also approved a capital raising plan of Rs. 10,100 crores. Currently, its Cost of Deposits (CoD) stand at 4.97% for Q1FY24, up 94/16bps YoY/QoQ. The management in the Concall specified that they are not very keen to hunt for bulky term deposits but might have to do so if the credit growth demands further liquidity in the bank. In such case, we can expect its CoD to be elevated.

	Q1FY24	Q4FY23	Q1FY23	YoY	QoQ
Current Account Balances	67,090	73,980	59,725	12%	-9%
Savings Account Balances	3,17,994	3,20,075	2,99,610	6%	-1%
CASA Balances	3,85,084	3,94,055	3,59,335	7%	-2%
Term Deposits	7,42,968	7,23,661	6,33,439	17%	3%
Total Deposits	11,28,052	11,17,716	9,92,774	14%	1%

(Source: Company, HDFC sec)



Digitization journey has started

The Bank has made significant inroads into digitization in the last couple of years. It has launched Sambhav- the bank's digital transformation project and has planned to invest Rs.1500 Cr on digitization initiatives for bringing next generation digitized consumer financial services. It has implemented many Digital Initiatives e.g. Pre- Approved Personal Loan (PAPL), MSME STP, MSME credit card, CRM Package, Trade Finance Module, UVConnect, Union Dial and the most recently Union Nxt – a new age super app for all banking needs. The bank has also expanded its footprint by opening 'smaller, sales-oriented digital branches' which are named as Digi-Connect & Digi-Connect Pro outlets. The idea behind the digital initiatives of the bank is to create a digital ecosystem where it actively engages with the customers so that it becomes a prime bank for its customers and thereby aid in higher business, higher CASA balance, higher transaction and overall higher profitability as well as saving on the opex.

To put in numbers, UBI has now been ranked 3rd in UPI transactions among all Public Sector Banks in the country. As of Q1FY24, the bank has 2.25 crore mobile banking users and ~164 crore UPI transactions were done during the quarter. These digital initiatives are also bringing in credit growth i.e. it has sanctioned 31% of the personal loans digitally, 94% of MSME Renewal <10 lacs done through STP (Straight Through Processing), 80% of the retail loans are reviewed digitally, 65% YoY growth in fixed deposits amount sourced digitally, 1 lakh plus CBDC retail user registrations during Q1FY24.

The bank is expected to transition its existing mobile banking platform to a new revamped one by the end of FY24. It is also expecting their digital contact centers to be up and running by the end of FY24. The key differentiator from the current call centers to the digital contact centers will be that while the current call centers is mostly responding to the inbound calls, the digital contact center actually be a sales and services center for the bank and will serve as a business generation engine for the bank.

Risks & Concerns

- Any unfavorable change in rules and regulatory policies can have a negative impact on earnings outlook of the Bank.
- Lower than expected business growth or sharp rise in slippages due to economic slowdown could result in deterioration in capital. Progress on recoveries will be important point to watch out in coming quarters.
- A sharp rise in interest rate could also result in MTM losses on its investment portfolio.
- Any further delay in the resolution of large assets due to current uncertainties and extension granted under IBC can postpone recoveries.
- The bank has CASA ratio at 34.6%, which is lower than industry average. This deteriorated further in Q1FY24 quarter, with 160 bps dip YoY basis and 102 bps dips on QoQ basis. This has had an impact on its cost of deposits as well which has increased by 94/16 bps YoY/QoQ. However, the management has changed focus towards building CASA and expects the ratio to improve going ahead. We shall closely watch the movement in the CASA ratio of the bank going forward.

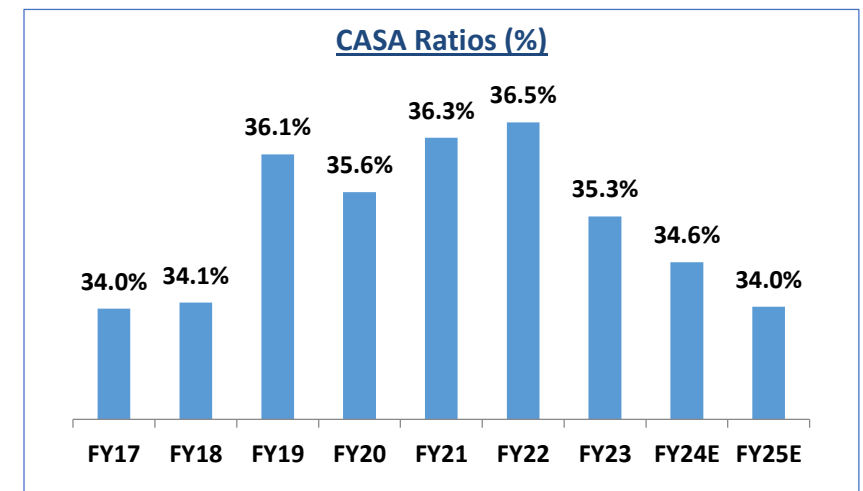
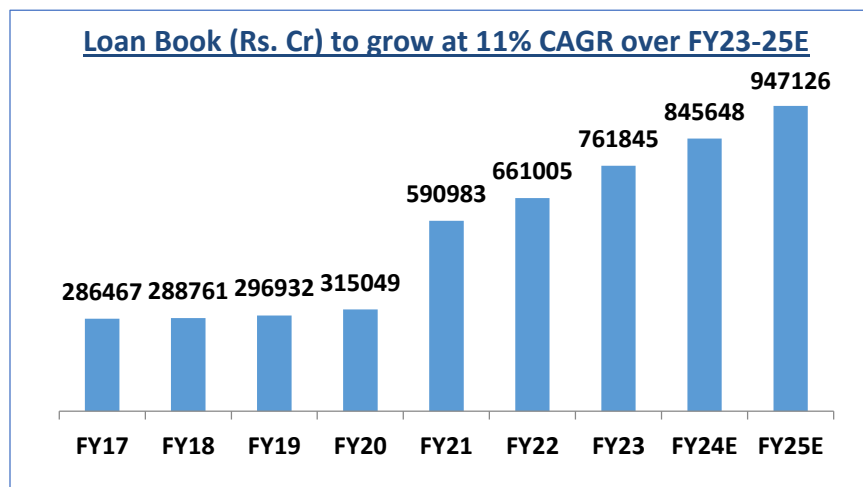


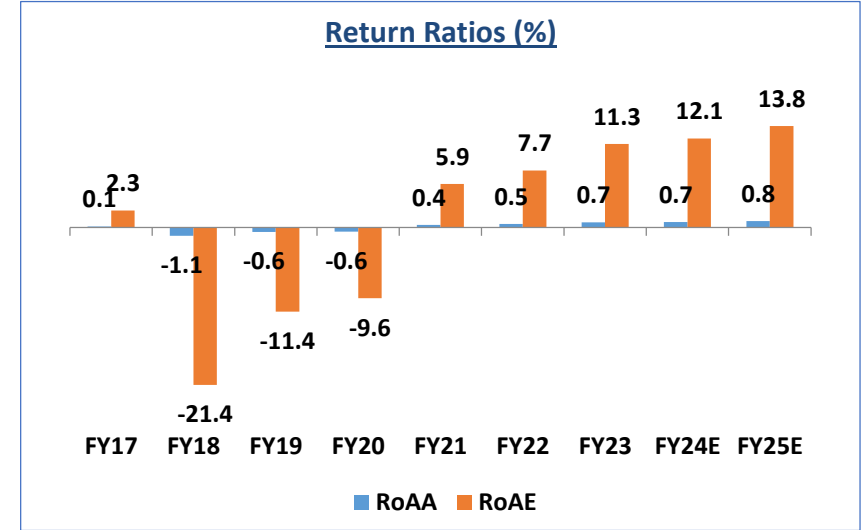
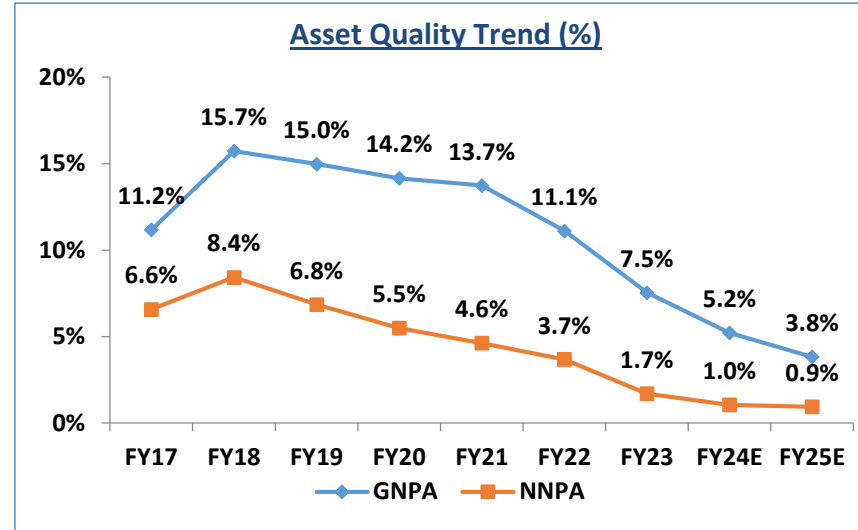
- The Government is holding 83.5% stake in the bank. This has to be brought down to 75% (SEBI’s minimum public shareholding). The board has approved a capital raising plan of Rs. 10,100 crores, which consists of Rs. 5,000 crores worth of QIP. This may pressurize the stock prices for some time.
- Though the management sounded confident that transitioning to the ECL provisioning regime will not be a problem considering their improved underwriting standards and aggressive provisioning in the past, we will remain watchful regarding new regulatory developments in this aspect.

Company Background:

Union Bank of India (UBI), established in 1919, is one of the oldest and largest public sector banks (PSBs) in India. Post amalgamation with Andhra Bank and Corporation bank with itself effective from April 1, 2020, the bank has emerged as the 5th largest in terms of total business and 4th largest in terms of network among the PSBs. Government of India (GOI) is the majority shareholder holding 83.49% stake as on June 30, 2023. As of Q1FY24, the bank has 8,561 branches and 10,195 ATMs. The bank has 3 overseas branches at Hong Kong, Dubai International Financial Centre (UAE) & Sydney (Australia); 1 banking subsidiary at London (UK); 4 parabanking subsidiaries (domestic); 2 other joint ventures (including in life insurance business) and 1 associate - Chaitanya Godavari Gramin Bank.

The bank’s principal banking and financial products and services include fund-based and non-fund-based facilities for corporate/ wholesale, retail, agriculture and micro, small and medium enterprises (“MSMEs”) customers. UBI also provides asset management services through its subsidiary, Union Asset Management Company Private Limited, broking services via UBI Services Limited and life insurance products through joint ventures i.e. Star Union Dai-ichi Life Insurance Company Limited and India First Life Insurance.





(Source: Company, HDFC sec)

Financials

Income Statement

Particulars	FY21	FY22	FY23	FY24E	FY25E
Interest Income	68767	67944	80743	86403	97706
Interest Expenses	44079	40157	47978	50910	57988
Net Interest Income	24688	27786	32765	35493	39718
Non interest income	11744	12525	14633	14467	16135
Operating Income	36433	40311	47398	49960	55853
Operating Expenses	16766	18438	21931	23554	25366
PPP	19667	21873	25467	26406	30487
Prov & Cont	17268	13294	13329	13063	13585
Profit Before Tax	2399	8579	12138	13344	16902
Tax	-507	3347	3704	3403	4310
PAT	2906	5232	8433	9941	12592

Balance Sheet

Particulars	FY21	FY22	FY23	FY24E	FY25E
Share Capital	6407	6835	6835	6835	6835
Reserves & Surplus	58070	63741	71499	79390	89589
Shareholder funds	64477	70576	78334	86224	96424
Deposits	923805	1032393	1117716	1217787	1357524
Borrowings	51837	51179	43137	54967	56828
Other Liab & Prov.	34854	36643	41564	45720	47549
SOURCES OF FUNDS	1074973	1190791	1280751	1404699	1558325
Cash & Bank Balance	84410	119500	112149	133909	149146
Investment	331512	348507	339299	347781	375604
Advances	590983	661005	761845	845648	947126
Fixed Assets	7344	7191	8826	9709	10679
Other Assets	60724	54587	58632	67652	75770
TOTAL ASSETS	1074973	1190791	1280751	1404699	1558325

(Source: Company, HDFC sec)



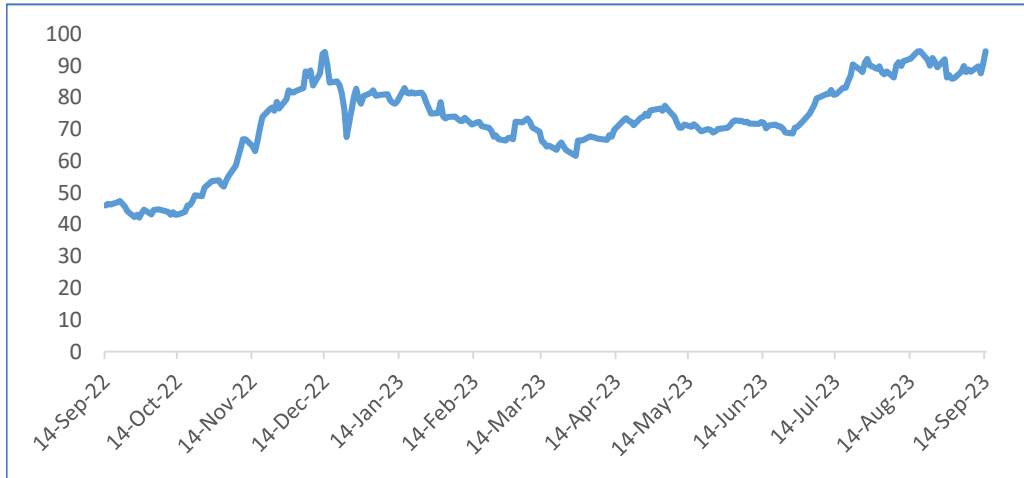
Key Ratios

Particulars	FY21	FY22	FY23	FY24E	FY25E
Return Ratios					
Calc. Yield on adv	11.6%	10.3%	10.6%	10.8%	10.9%
Calc. Cost of funds	4.5%	3.7%	4.1%	4.0%	4.1%
NIM	2.9%	2.7%	2.9%	2.9%	3.0%
RoAE	5.9%	7.7%	11.3%	12.1%	13.8%
RoAA	0.4%	0.5%	0.7%	0.7%	0.8%
Asset Quality Ratios					
GNPA	13.7%	11.1%	7.5%	5.2%	3.8%
NNPA	4.6%	3.7%	1.7%	1.0%	0.9%
PCR	69.6%	69.5%	78.8%	80.0%	75.7%
Growth Ratios					
Advances	87.6%	11.8%	15.3%	11.0%	12.0%
Deposits	105.0%	11.8%	8.3%	9.0%	11.5%
NII	115.9%	12.5%	17.9%	8.3%	11.9%
PAT	-200.3%	80.0%	61.2%	17.9%	26.7%

Key Ratios

Particulars	FY21	FY22	FY23	FY24E	FY25E
Valuation Ratios					
EPS	4.5	7.7	12.3	14.5	18.4
P/E	20.8	12.3	7.7	6.5	5.1
Adj. BVPS	45.1	55.6	83.6	101.2	116.1
P/ABV	2.1	1.7	1.1	0.9	0.8
Dividend per share	0.0	1.9	3.0	3.0	3.5
Other Ratios					
Cost-Income	46.0	45.7	46.3	47.1	45.4
CASA	36.3	36.5	35.3	34.6	34.0
CAR	12.6	14.5	16.0	15.9	15.8
Tier 1	10.4	12.2	13.9	14.0	14.1

One Year Price Chart





HDFC Sec Retail Research Rating description

Green Rating stocks

This rating is given to stocks that represent large and established business having track record of decades and good reputation in the industry. They are industry leaders or have significant market share. They have multiple streams of cash flows and/or strong balance sheet to withstand downturn in economic cycle. These stocks offer moderate returns and at the same time are unlikely to suffer severe drawdown in their stock prices. These stocks can be kept as a part of long term portfolio holding, if so desired. This stocks offer low risk and lower reward and are suitable for beginners. They offer stability to the portfolio.

Yellow Rating stocks

This rating is given to stocks that have strong balance sheet and are from relatively stable industries which are likely to remain relevant for long time and unlikely to be affected much by economic or technological disruptions. These stocks have emerged stronger over time but are yet to reach the level of green rating stocks. They offer medium risk, medium return opportunities. Some of these have the potential to attain green rating over time.

Red Rating stocks

This rating is given to emerging companies which are riskier than their established peers. Their share price tends to be volatile though they offer high growth potential. They are susceptible to severe downturn in their industry or in overall economy. Management of these companies need to prove their mettle in handling cyclicity of their business. If they are successful in navigating challenges, the market rewards their shareholders with handsome gains; otherwise their stock prices can take a severe beating. Overall these stocks offer high risk high return opportunities.

Disclosure:

I, **Varun Nitin Manek**, Research Analyst, (ACA), authors and the names subscribed to this report, hereby certify that all the views expressed in this research report accurately reflect our views about the subject issuer(s) or securities. SEBI conducted the inspection and based on their observations have issued advise/warning. The said observations have been complied with. We also certify that no part of our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report.

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Any holding in stock – No

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