

CSB Bank Ltd. – Management Meet

The Growth Agenda

We met the top management of CSB Bank recently to understand the future strategy and outlook in the medium to long term. The discussion was regarding the contours of the growth trajectory and the composition of the loan book, as well as operating cost transition in terms of branch expansion and technology investments.

The management has sketched out a plan for the short term (<3 years), medium term (5 years) and long term (10 years). The immediate focus of the management was on the following points:

- a) Strengthen the technology backbone of the bank, for which the company has hired a Chief Technology Officer with extensive experience in the banking sector.
- b) Enhance fee income by forming robust partnerships with aggregators, insurers, brokers, fintech players, dealers and AMCs.
- c) Create a granular liability franchise through customer acquisition and opening of more liability branches. To achieve this, the bank will double its employee base to ~10k over the next 2-3 years.

Over the long term, the management aims to create pan India presence as the economy will require more banks. Of the existing ones, the management expects only 2–3 banks to grow to a larger scale than the top 7-8 banks. CSB’s aim is to create the right franchise rather than focusing on specific growth numbers, as the right franchise will eventually result in industry leading growth.

Long-term target of 1.5x of industry growth

The management is targeting to grow the asset book at 1.5x of industry growth. It has projected banking credit growth of 14–16% for the next three years, with GDP growth projection of 7–8%. MSME growth and return of corporate growth in the next 2–3 quarters are likely to boost credit growth in the near term. The management believes that Services, Consumption, EPC, Housing, CV&CE and Infrastructure will drive growth in the advances book. In addition, the management is expecting the corporate borrowing book to shift from overseas to the domestic banking system as the overseas borrowing rate is inching up.

The management is internally targeting 20%+ credit growth for the next three years, but this will accelerate after FY27 as the bank will have robust technology in place and a strong liability franchise to support the credit growth. Moreover, the management is planning to get into the credit card business through a partnership and introduce more retail products in due course. In the short term, the gold loan book will remain the growth driver for the bank. In the long term, however, the bank’s book will be more diversified. The share of gold loans will reduce from the current 40% to 25%; the retail book will represent 25%, SME will account for 20–22% and the corporate book will constitute the rest. In terms of inorganic growth, the management believes it may be worthwhile to acquire a portfolio or a specific book in order to complement the organic growth as planned.

Renewed focus to boost fee income through increased cross-selling and customer acquisition

The bank seeks to enter into robust partnerships that would help generate a sustainable stream of fee income. At present, the bank has about 1.5mn customers; of this, two-third of the base is not adding value on the wealth income front. In addition, CSB intends to acquire quality customers through multiple tie-ups, which would result in increased cross-selling opportunities.

Investments to keep opex elevated in near term

Investments in technology are likely to remain high for the next few quarters. This, coupled with aggressive branch opening and hiring (employee count is expected to almost double over the next 2–3 years), is expected to keep operating expenditure elevated in the near term.

Outlook and valuation

At CMP, the stock is trading at 0.9x FY24E ABV. The bank has industry leading margins, strong return ratios and robust asset quality. With anticipated credit growth of nearly 20% during FY22–24E, we expect a re-rating. **As such, we maintain our ‘BUY’ recommendation with TP of INR340/share, implying an 89% upside.**

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CMP: INR 180

Rating: BUY

Target price: INR 340

Upside: 89%

Date: June 16, 2022

Bloomberg:	CSB:IN
52-week range (INR):	180 / 374
M-cap (INR crore):	3,175
Promoter holding (%)	49.72

Year to March (INR cr)	FY20	FY21	FY22	FY23E	FY24E
Net revenue	814	1,342	1,400	1,611	1,900
PPoP	281	613	614	700	870
PAT	13	218	457	398	498
Diluted EPS (INR)	0.7	12.6	26.4	23.0	28.7
Adjusted Book Value (INR)	108.0	121.8	150.3	171.4	197.7
Return on Equity (%)	0.9%	10.5%	18.9%	14.1%	15.3%
Price-to-Earnings (x)	251.3	14.6	7.0	8.0	6.4
Price-to-Adjusted BV (x)	1.7	1.5	1.2	1.1	0.9

CSB Bank Ltd. – Management Meet

The Growth Agenda

Growth expected to be prioritised at the expense of marginal profitability hit in near term

CSB is generating its highest net interest margin in the banking system, largely due to the high share of gold loans in its asset mix, while cost of funds also moderated substantially compared to peers. Cost of funds declined 386 bps over the past six years as the bank improved its CASA ratio from 20% in FY16 to 34% currently. The management expects margins to normalise as the focus is likely to shift to other lower yielding products. In the short term, we expect lower margins and higher opex to weigh on the return ratios of the bank.

Management track record – Mr. Pralay Mondal

We met Mr. Pralay Mondal, who is the interim CEO and Managing Director of CSB Bank. Mr. Mondal has 30 years of banking experience in multiple businesses and functions including retail assets and liabilities, business banking, product and technology. He previously worked as Executive Director and Head of Retail Banking in Axis Bank. Before joining Axis Bank, he was Senior Group President and Head of Retail and Business Banking at Yes Bank. Mr. Mondal was instrumental in setting up the entire retail franchise in that bank in a short period of time. Prior to that, he did a successful 12 years' stint at HDFC Bank and was earlier associated with Standard Chartered Bank, Wipro InfoTech and Colgate Palmolive.

Mr. Mondal's achievements include pioneering efforts in doorstep banking and direct sales, creating deep geography distribution as well as building and scaling up retail businesses. He is also credited with building capital markets, wealth management, private banking, NBFCs, credit cards, payments and digital businesses from scratch.

Given his background and experience, we believe that Mr. Mondal has rich expertise in creating large retail-focused books and a strong liability franchise from the ground up while maintaining the asset quality standard, which has stood the test of a challenging environment. This augurs well for CSB as the company starts its transition to becoming a mid-sized diversified bank with a robust deposit franchise.

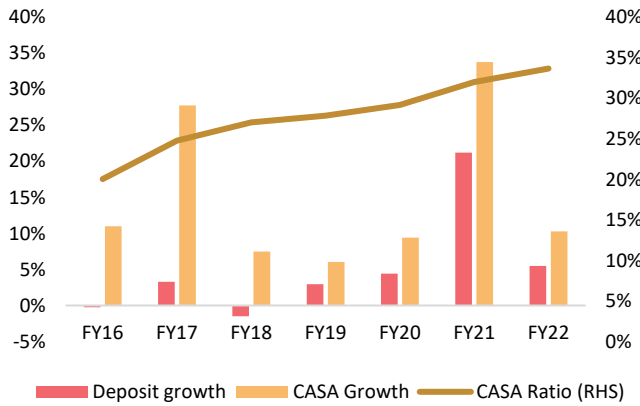
Key Risks:

- A general weakening of the macroeconomic scenario over the next couple of years could impact CSB's ability to scale up its loan book.
- The anticipated rapid credit growth is contingent on retention of the current top management team over the medium to long term. Any substantial exit in the key management may impact our projection and target.

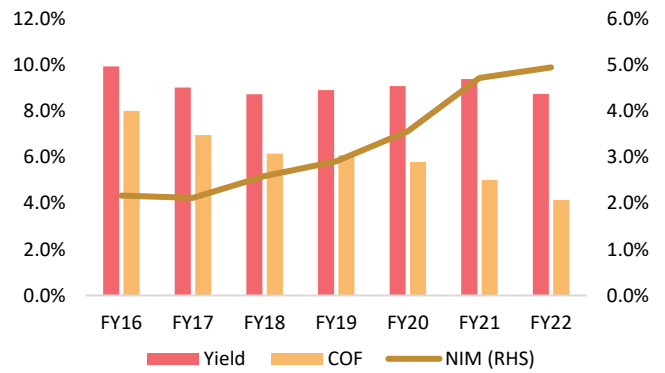
CSB Bank Ltd. – Management Meet

The Growth Agenda

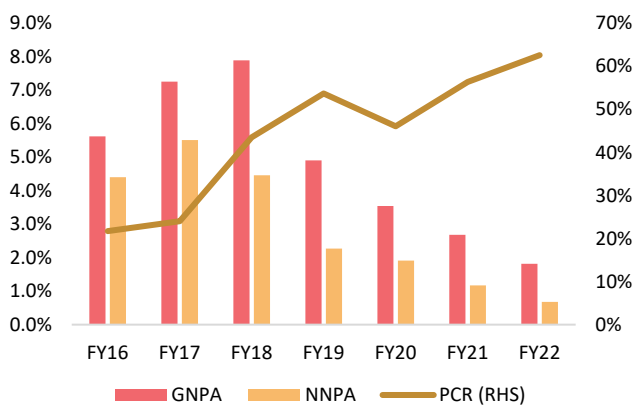
Impressive CASA growth drives overall deposits



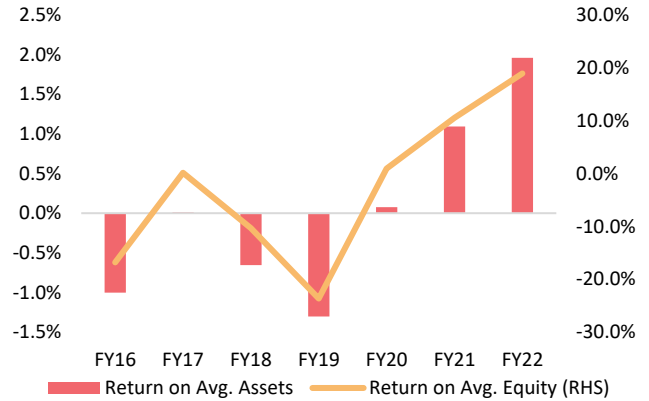
Substantial declines in CoF lead to strong uptick in NIM



Improvement in asset quality continues



Improvement in return ratios sustained



Source: Edelweiss Wealth Research

CSB Bank Ltd. – Management Meet

The Growth Agenda

Key Managerial Personnel

Name	Role	Background
Pralay Mondal	<i>Interim MD & CEO</i>	Mr. Mondal holds an Engineering degree from IIT Kharagpur and is a management graduate from IIM Kolkata. He has three decades of banking experience across various products and functions such as retail, business banking, products and technology. Prior to joining CSB, he was the Head of Retail Banking at Axis Bank. He has also held senior positions at Yes Bank (Head of Commercial Business Banking and Rural Banking) and HDFC Bank (Head of Retail Assets and Credit Cards).
B K Divakara	<i>Chief Financial Officer</i>	Mr. Divakara holds a bachelor's degree in Business Management from University of Mysore. Further, he is an Associate of the Institute of Chartered Accountants of India and Associate of the Institute of Company Secretaries of India. He is also an associate of Institute of Cost and Management Accountants of India. Prior to joining CSB Bank, he was working with the Central Bank of India as Executive Director and Corporation Bank and has over 36 years of experience in the field of banking. He has varied and rich experience in Treasury, Credit and Operations.
Narendra Dixit	<i>Head – Retail Banking</i>	Mr. Dixit has over 22 years of banking experience and was recently appointed by CSB. Prior to joining CSB, he was the National Head of Liability Sales at Axis Bank. He was also Group President of Branch Banking at Yes Bank, where he played a key role in building the bank's acquisition channel and strategy.
Shyam Mani	<i>Head – SME and NRI</i>	Mr. Mani holds a degree in Engineering from Bangalore University and has 24 years of banking experience across various functions such as branch banking, retail banking, SME and NRI banking. He was recently appointed by CSB. Prior to his current role, he headed the NRI Banking division at Yes Bank. He has also been associated with ICICI Bank and HDFC Bank.
Rajesh Choudhary	<i>Chief Technology Officer</i>	Mr. Choudhary has almost three decades of experience in technology leadership roles. His work exposure spans Europe, the UK, the UAE, Singapore and India. Prior to joining CSB, he was associated with Barclays Bank, RBS, ICICI Bank and Bank of America.
Manish Agarwal	<i>Chief Credit Officer</i>	Mr. Agarwal holds a Chartered Accountant, Cost Accountant and CS(Inter) degree. He has over 25 years of experience in managing risk in Banking & NBFC sector. Prior to joining CSB Bank, he was associated with U GRO Capital where he was holding the position of Chief Risk Officer (CRO). Prior to U GRO Capital he has worked with YES Bank as Chief Credit Officer (Retail and Agri), ICICI Bank in various roles, with last role as Head Policy – Retail, Agri & SME. He has also worked in Kotak Mahindra Primus Ltd and PwC.
Harsh Kumar	<i>Chief Human Resources Officer</i>	Mr. Kumar holds a bachelor's degree in engineering from University of Madras and a post graduate diploma in management from T.A. Pai Management Institute. He has over 15 years of experience in the field of banking. Prior to joining CSB Bank, he was associated with HDFC Bank Limited.

Source: Edelweiss Wealth Research

CSB Bank Ltd. – Management Meet

The Growth Agenda

Financials

Income Statement (INR cr)

Year to March	FY20	FY21	FY22	FY23E	FY24E
Interest income	1,510	1,872	2,038	2,350	2,795
Interest charges	918	931	885	1,081	1,331
Net interest income	592	941	1,153	1,268	1,464
Other income	222	401	247	343	436
Net revenues	814	1,342	1,400	1,611	1,900
Operating expense	534	729	786	911	1,030
- Employee exp	331	496	482	565	634
- Depreciation / amortisation	24	-	-	-	-
- Other opex	179	233	305	346	397
Preprovision op. profit	281	613	614	700	870
Provisions	147	321	1	166	202
PBT	134	293	613	534	668
Taxes	121	74	156	136	170
PAT	13	218	457	398	498
Extraordinaries	-	-	-	-	-
Reported PAT	13	218	457	398	498
Basic number of shares (cr.)	17	17	17	17	17
Basic EPS (INR)	0.7	12.6	26.4	23.0	28.7
Diluted number of shares (cr.)	17	17	17	17	17
Diluted EPS (INR)	0.7	12.6	26.4	23.0	28.7

Growth Ratios

Year to March	FY20	FY21	FY22	FY23E	FY24E
NII growth	35%	59%	23%	10%	15%
Non Interest Income growth	63%	81%	-38%	39%	27%
Net Revenues growth	41%	65%	4%	15%	18%
Opex growth	-5%	37%	8%	16%	13%
PPOP growth	1994%	119%	0%	14%	24%
Provisions growth	-53%	119%	-100%	32453%	22%
PAT growth	-106%	1620%	109%	-13%	25%

Operating Ratios

Year to March	FY20	FY21	FY22	FY23E	FY24E
Yield on Average Advances	10.6%	10.7%	10.6%	10.6%	10.6%
Yield on Investments	6.6%	8.0%	5.8%	6.3%	6.5%
Yield on interest earning assets	9.1%	9.4%	8.7%	8.9%	9.0%
Cost of Funds	5.8%	5.0%	4.1%	4.5%	4.7%
Spread	3.3%	4.4%	4.6%	4.4%	4.3%
Net Interest Margin	3.6%	4.7%	4.9%	4.8%	4.7%
Cost to Income Ratio	65.5%	54.3%	56.2%	56.5%	54.2%
Tax Rate	90.5%	25.3%	25.4%	25.4%	25.4%

CSB Bank Ltd. – Management Meet

The Growth Agenda

Balance Sheet (INR cr)

As on 31st March	FY20	FY21	FY22	FY23E	FY24E
CAPITAL AND LIABILITIES					
Share Capital	173	173	174	174	174
Reserves and Surplus	1,787	2,007	2,478	2,845	3,302
Warrants	-	-	-	-	-
Deposits	15,791	19,140	20,188	23,729	28,239
Borrowings	794	1,426	2,007	2,136	2,542
Other Liabilities & Provisions	319	591	509	482	1,015
Total Liabilities	18,864	23,337	25,356	29,365	35,271
ASSETS					
Cash and Balances with RBI	548	736	948	1,305	1,412
Balances with Banks & Call Money	392	978	626	949	1,130
Investments	5,360	6,126	7,012	7,593	9,037
Advances	11,366	14,438	15,814	18,447	22,421
Fixed Assets	228	270	288	302	311
Other Assets	970	790	668	769	961
Total Assets	18,864	23,337	25,356	29,365	35,271

Balance sheet ratios (%)

Year to March	FY20	FY21	FY22	FY23E	FY24E
Loan growth	7%	27%	10%	17%	22%
IEA growth	13%	26%	10%	16%	20%
Deposits growth	4%	21%	5%	18%	19%
IBL growth	10%	24%	8%	17%	19%
Gross NPA ratio	3.5%	2.7%	1.8%	1.6%	1.5%
Net NPA ratio	1.9%	1.2%	0.7%	0.6%	0.5%
Provision coverage	46%	56%	63%	62%	66%
CAR	22%	21%	26%	25%	24%

RoAE Decomposition

Year to March	FY20	FY21	FY22	FY23E	FY24E
Net Interest Income / Assets	3.6%	4.7%	4.9%	4.8%	4.7%
Other Income / Assets	1.3%	2.0%	1.1%	1.3%	1.4%
Net Revenues / Assets	4.9%	6.7%	6.0%	6.1%	6.1%
Operating Expense / Assets	3.2%	3.7%	3.4%	3.5%	3.3%
Provisions / Assets	0.9%	1.6%	0.0%	0.6%	0.6%
Taxes / Assets	0.7%	0.4%	0.7%	0.5%	0.5%
Total Costs / Assets	4.8%	5.6%	4.0%	4.6%	4.5%
Return on Assets	0.1%	1.1%	2.0%	1.5%	1.6%
Assets / Equity	12.1	9.6	9.7	9.3	9.6
Return on Average Equity	0.9%	10.5%	18.9%	14.1%	15.3%

Valuation Metrics

Year to March	FY20	FY21	FY22	FY23E	FY24E
Basic EPS	0.7	12.6	26.4	23.0	28.7
EPS growth	-1.0	16.2	1.1	-0.1	0.3
Adjusted book value per share	108.0	121.8	150.3	171.4	197.7
Basic P/E	251.3	14.6	7.0	8.0	6.4
Price - to - Book	1.7	1.5	1.2	1.1	0.9

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