

## CENTURION BANK OF PUNJAB

INR 23

CBOP and LKB to merge

BUY

The boards of Centurion Bank of Punjab (CBOP) and Lord Krishna Bank (LKB) have agreed in-principle to merge both the banks. The transaction is subject to agreement on valuation and approval from RBI.

We believe LKB acquisition will be positive for CBOP considering:

- ◆ CBOP's presence in southern India will be enhanced with an addition of 112 branches
- ◆ CBOP's ability to integrate business successfully
- ◆ CBOP stands to gain in an all share swap deal, given its current premium valuations (2.9x book)

In terms of balance sheet growth, the proposed acquisition will add only 21% (when CBOP is growing 15% Q-o-Q), but it will lead to 45% expansion in branch network.

Lord Krishna Bank is a closely held private sector bank with 65% of the equity lying with the promoter Mr. Mohan Puri. The Burmans of Dabur hold 5% in LKB. The Puris have been under pressure from RBI to dilute their holding for quite some time. This merger gives them an appropriate opportunity to pare their holding to more acceptable level. The bank had been under capital constraint as it strived to meet RBI's minimum net worth requirement of INR 3.0bn and was planning to come out with an IPO during this fiscal.

LKB has 112 branches in all with 69 of them being in Kerala. Centurion bank is predominantly present in western and northern India. The proposed merger would further enhance CBOP's presence in southern India. The branch network of merged entity would increase to over 360 from 249 (of CBOP).

**Table 1: LKB would add 20% to balance sheet**

INR mn	CBOP	Lord Krishna	LKB as % of CBOP	Merged
Advances	74,524	14,209	19	88,733
Deposits	103,721	22,789	22	126,510
Balance sheet size	124,809	25,993	21	150,802
Branches	249	112	45	361

Source: Company reports, Edelweiss research

#### Financials

Year to March	FY05	FY06E	FY07E	FY08E
Revenues (INR mn)	4,755	7,202	9,468	13,141
Rev growth (%)	(1.5)	51.5	31.5	38.8
Net interest income (INR mn)	3,128	3,988	5,474	7,974
Net profit (INR mn)	(186)	878	1,455	2,520
Shares outstanding (mn)	128.0	140.8	163.5	163.5
EPS (INR)	(0.1)	0.6	0.9	1.5
EPS growth (%)	(82.2)	(528.0)	42.7	73.2
PE (x)	(160.7)	37.5	26.3	15.2
Price to book (x)	5.5	3.6	2.3	2.1
ROE (%)	(5.0)	12.9	11.4	14.6

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Reuters : CENB.BO  
 Bloomberg : CBOP IN

#### Market Data

52-week range (INR) : 31 / 16  
 Share in issue (mn) : 147.8  
 M cap (INR bn/USD mn) : 3.5 / 74.5  
 Avg. Daily Vol. BSE/NSE ('000) : 1,157.6

#### Share Holding Pattern (%)

Promoters : 0.0  
 MFs, Fls & Banks : 2.2  
 Fls : 19.5  
 Others : 78.3



The current margins (around 2%) and profitability (ROE of less than 2%) of LKB are singularly not attractive enough. However we believe once the high yield loan products and fee based services of CBOP are pushed through LKB branches its profitability would improve.

We believe that fair value for LKB should be close to 2.0x FY06 book considering the branch network and present valuations of CBOP. At INR 3.28bn valuations CBOP would be paying INR 29mn per branch for LKB's network of 112 branches, as LKB has lower NPAs than erstwhile Bank of Punjab. CBOP had paid INR 25mn per branch valuation to acquire Bank of Punjab, which had a network of high CASA deposit branches in Northern India.

**Table 2: Valuation scenario**

Valuations scenario (LKB)	1	2	3
Price to book	1.8	2.0	2.2
Net worth	1,638	1,638	1,638
Value for LKB stake	2,948	3,276	3,604
Price per branch	26.3	29.3	32.2
Required CBOP dilution	9.5	10.5	11.6
P/B merged entity	2.6	2.6	2.6

Source: Company reports, Edelweiss research

M/s Deloitte Haskins & Sells and M/s N M Rajji & Co. have been appointed to calculate fair value of the LKB, we believe it should be valued close to 2.0x FY06 book.

Assuming the deals go through at current valuations of CBOP, the merged entity will trade at 2.6x FY07E book.

Proposed merger is in line with CBOP's plans to grow inorganically, and we are confident about successful business integration post merger, given CBOP's ability to handle post acquisition process (Bank of Punjab merger).

**Table 3: Branch network**

	LKB	Centurion	Merged
Branches & extrn. counters	112	249	361
Geographic presence in			
<i>North &amp; East</i>	19.6	65.1	51.0
<i>South &amp; West</i>	80.4	34.9	49.0
No of employees	1,220	4,471	5,691

Source: Company reports, Edelweiss research

**Table 4: Branch locations**

<u>Locations</u>	<u>LKB</u>	<u>Centurion Branch+Extn</u>	<u>Post Merger</u>
Jammu	0	1	1
Punjab	5	65	70
Haryana	2	18	20
Chandigarh	1	8	9
Rajasthan	1	11	12
Gujarat	1	11	12
Maharashtra	8	23	31
Karnataka	5	11	16
Goa	0	6	6
Kerala	69	14	83
TN	5	19	24
Andhra	2	4	6
MP	0	5	5
Orrisa	0	1	1
Bihar	0	1	1
WB	0	9	9
Delhi	11	36	47
UP	2	5	7
Uttaranchal	0	1	1
	<b>112</b>	<b>249</b>	<b>361</b>

*Source: Company reports, Edelweiss research*

The proposed merger is in line with our expectations, and though it may not be EPS accretive in FY07, it would add to earnings from FY08 once CBOP starts marketing its product basket through LKB branches. The CBOP stock currently trades at 2.9x FY07E book (pre-merger) and 2.6x book (post merger), we reiterate **'BUY'**. LKB is an unlisted entity.

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Ashutosh Goel - 2286 4287	Automobiles, Auto Components	Shabnam Kapur - 2286 4394
Vishal Goyal - 2286 4370	Banking & Finance	Ashish Maheshwari - 2286 4418
Revathi Myneni - 2286 4413	Cement	Amish Choksi - 2286 4201
Sumeet Budhraj - 2286 4430	FMCG, Power	Deepak Rao - 2286 4204
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Hitesh Zaveri - 2286 4424	Information Technology	Monil Bhala - 2286 4400
Pritesh Vinay - 2286 4429	Metals, Mining	Ashish Agrawal - 2286 4301
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Pakhi Jain - 2286 4427	Pharmaceuticals, Agrochemicals	Anubhav Kanodia - 2286 4361
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### RATING INTERPRETATION

<b>Buy</b>	Expected to appreciate more than 20% over a 12-month period	<b>Reduce</b>	Expected to depreciate up to 10% over a 12-month period
<b>Accumulate</b>	Expected to appreciate up to 20% over a 12-month period	<b>Sell</b>	Expected to depreciate more than 10% over a 12-month period
<b>Trading Buy</b>	Expected to appreciate more than 10% over a 45-day period	<b>Trading Sell</b>	Expected to depreciate more than 10% over a 45-day period

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