

Karur Vysya Bank Ltd.



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Changing focus towards retail lending

CMP INR 75	Target INR 83	Potential Upside 10.6%	Market Cap (INR Mn) 59,708	Recommendation Accumulate	Sector Banking
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Result highlights

- Advances grew during Q4FY19 at 8.4% YoY/1.71% QoQ. Deposit mobilization was slow with a growth of 5.2% YoY/2.1% QoQ.
- NII at INR 619 Cr. is down 3.7% YoY/ up 6.6% QoQ. NIMs stood at 3.89%, a decline of 24 bps YoY/ up 32 bps QoQ. Total Income at INR 892 Cr. is up 4.7% YoY/6.1% QoQ. PPOP at INR 465 Cr is down 3.1% YoY/ up 9.4% QoQ on back of declining NIMs.
- The bank has provided for INR 352 Cr of net provisions during the quarter, down 10.6% YoY/ down 12% QoQ translating in credit costs of 4.18%, an increase of 174 bps YoY / 1 bps QoQ.
- Asset quality improved with GNPA at 8.79%, increasing by 223 bps YoY / 30 bps QoQ while NNPA at 4.98% was 82 bps higher on annual basis and 1 bps better sequentially. PCR stood at 56.9%.
- PAT at INR 60 Cr is up by 18% YoY/ 183% QoQ, translating into ROA of 0.35% on account of lowering of provisions.
- The board declared dividend of INR 0.60 per equity share of face value of INR2 for FY19.

MARKET DATA

Shares outs (Mn)	799
Equity Cap (INR Mn)	64,288
Mkt Cap (INR Mn)	59,708
52 Wk H/L (INR)	63/100
Volume Avg (3m K)	15,500
Face Value (INR)	2
Bloomberg Code	KVB IN

KEY FINANCIALS

Particulars (INR Crores)	FY17	FY18	FY19	FY20E	FY21E
NII	2,074	2,298	2,363	2,520	2,786
PPOP	1,571	1,777	1,711	1,751	1,884
PAT	606	345	211	281	410
EPS	9.95	4.75	2.64	3.52	5.13
NIM	3.6%	3.7%	3.5%	3.4%	3.5%
Advances Growth	4.7%	9.5%	8.4%	9.0%	10.0%

Source: Company, KRChoksey Research

Retail book driving lending growth; Slow mobilization of deposits

Karur Vysya Bank's advances grew by 8.4% during FY19 on the back of high growth in retail segment which grew by 24%. Among the personal loans segment, the housing loans increased by 29.5% and others retail loans grew by 182% reflecting the bank's focus shifting towards retail segment assets while vehicle loans remained flat due to slowdown in overall auto sector sales. The commercial loans grew by 6% in FY19 while corporate loans declined by 2% as preference for higher rated loans was observed. The jewellery segment loans also grew by 10% in FY19. On the deposit side, the CASA ratio stood at 30% of the total deposits, with growth in savings account by 10%. The term deposits grew by 4% only and constituted 70% of the deposits of which 93% were less than INR 5 Cr accounts, acknowledging the high cost of funds for the bank.

Slower growth in NII and operating profits; gradual expansion of NIMs on increased costs

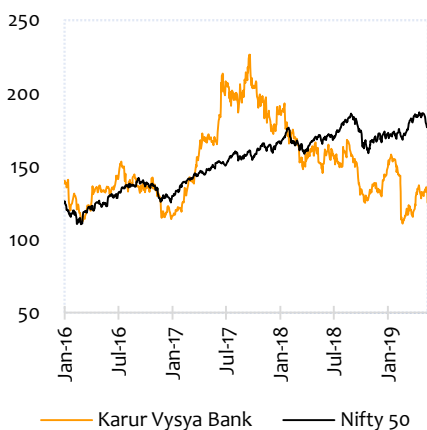
NII grew by 2.82% for FY19, while the operating profits dipped by 3.7% due to rising costs for the bank. The non-interest income grew by 7% during the year, and is expected to contribute higher in the coming future as the bank shifts its focus towards retail assets.

Asset quality improved as heavier provisioning continued on stressed books

Asset quality degraded further during the year as the bank had to recognize several NPA accounts as provisions for the year rose to INR 1,389 Cr against last year's INR 1,274 Cr. The GNPA increased from 6.57% in FY18 end to 8.79% in FY19 and the NNPA rose from 4.16% to 4.98% in FY19. In the commercial loan segment, 80% accounts are for less than INR 5 Cr ticket size while in the corporate loan segment, 72% accounts are less than INR 100 Cr. In the corporate loan segment, the bank has reduced its books of manufacturing sector loans from 9.0% in FY18 to 8.4% in FY19 of total advances along with infrastructure loans down to 3.9% in FY19 from 6.1% in FY18 of total advances.

Overall the bank has started to show resilience against lending towards low rated corporate & commercial segments and is shifting towards retail loans of smaller tickets and housing loans which have very low risk and will also lead to increase in levels of standard assets.

SHARE PRICE PERFORMANCE

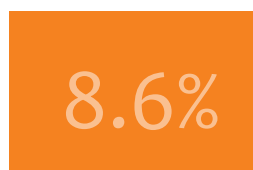


MARKET INFO

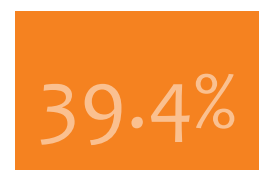
SENSEX	37,393
NIFTY	11,257

SHARE HOLDING PATTERN (%)

Particulars	Mar-19	Dec 18	Sep 18
Promoters	2.08	2.11	2.1
FIIs	18.12	17.38	17.94
DIIIs	23.69	23.49	21.05
Others	56.11	57.02	58.91
Total	100	100	100



NII CAGR between FY19 and FY21E



PAT CAGR between FY19 and FY21E

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Key Con-call Highlights: (i) Karur Vysya bank to focus on retail loan segment and aims to sustain the current growth rate of 24% (excl. APCA) in the next few years and lending is expected to remain tight for the other segments as per the asset quality. However, the bank aims to have around 5% of growth from the corporate and commercial loan segment as well but has preference for lesser risky assets. (ii) The bank has invested to set-up proper core banking infrastructure, which will help the bank to generate more API's. (iii) The bank has set up a new business banking unit to focus on commercial loans of INR3-15 Cr of token size and will be operational by end of May. (iv) The bank aims to provide provisions for INR1200 Cr for the next year and achieve a PCR of 60% as per the industry norms. (v) The bank has no exposure towards IL&FS and DHFL but has exposure of >100 Cr towards Reliance Telecom and the account is under watch. (vi) The bank has around INR 400-500 Cr of assets in NCLT process. (vii) Of the retail loan, the bank has 93% of the accounts less than INR 5 Cr of token size, and almost 80% of the retail loan accounts are of customers with bank accounts with the bank. (viii) **Future Guidance:** The management expects to achieve operating profits of INR 2000 Cr, make provisions of INR 1200 Cr and PBT of INR 800 Cr for FY20.

Valuation and view

We expect KVB Bank to deliver NII growth of average 8.6% YoY in FY20E/FY21E on back of its renewed focus towards retail business (network of 778 branches and 2,179 ATMs). The bank has good presence in the southern states and has more than 80% of the branches in metros, urban and semi-urban towns & cities, thereby has a very high potential to grow. Overall, we expect NIMs to average 3.4% in FY20/21. Increase in fee income should support the overall operating income growth (+8.4% average for FY20/21). Asset quality metrics are forecast to improve credit costs, which is expected to be ~2.25%, PCR at 60% and Net NPA expected to remain ~3.5% in the forecast period.

We expect the management to continue focus on retail loan segment in the coming future and the housing loans among it to drive the bulk of the growth in the next few years. However, apart from serving own bank account customers (since, 80% of retail loan customers are bank customers of KVB), the retail lending segment is highly competitive with other existing players exhibiting even faster growth, we believe the size of retail loan segment will take longer than the management's expectation. Hence, we foresee the assets to grow faster in the future with focus on retail, but tighter lending on corporate & commercial loan segment will keep the growth in the higher-single digits. **Karur Vysya Bank is currently trading at a P/Adj.BV multiple of 0.90x/0.81x on FY20E/FY21E adj. book value and we expect the valuation discount for the bank to continue on the back of weak ROE outlook (average 4.8% for FY20/21). We apply a P/Adj.BV multiple of 1.3x to the FY21 adj. BVPS of INR 66 to arrive at a target price of INR 83 per share, an upside of 10.6% over the CMP. Accordingly, we assign an "Accumulate" rating.**

KEY FINANCIALS

Exhibit 1: Profit & Loss Statement

INR Crores	FY 17	FY 18	FY 19	FY 20E	FY 21E
Interest Income	5,622	5,700	5,816	6,303	6,832
Interest Expense	3,549	3,402	3,453	3,783	4,046
Net Interest Income	2,074	2,298	2,363	2,520	2,786
Non interest income	782	900	963	1,040	1,123
Operating income	2,856	3,198	3,326	3,560	3,909
- Employee expense	608	639	761	853	955
- Other operating expense	677	782	854	956	1,071
Operating Expense	1,285	1,421	1,615	1,809	2,026
PPOP	1,571	1,777	1,711	1,751	1,884
Provisions	687	1,274	1,389	1,319	1,253
PBT	883	503	322	432	631
Tax Expense	277	158	111	151	221
PAT	606	345	211	281	410
Diluted EPS (INR)	9.95	4.75	2.64	3.52	5.13

Source: Company, KRChoksey Research

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Exhibit 2: Balance Sheet

INR Crores	FY17	FY18	FY19	FY20E	FY21E
Source of Funds					
Share capital	122	145	160	160	160
Reserves & Surplus	4,914	6,119	6,263	6,460	6,747
Networth	5,036	6,264	6,423	6,901	7,316
Borrowings	1,696	2,382	1,565	1,659	1,775
Deposits	53,700	56,890	59,868	63,460	67,902
Other liabilities & provisions	1,376	1,393	1,484	1,573	1,683
Total Equity & Liabilities	61,808	66,929	69,340	73,593	78,677
Uses of Funds					
Cash & Balances w/ RBI	2,790	2,960	2,935	3,640	3,052
Balances with Other Banks	1,555	1,337	762	839	922
Investments	14,857	15,803	14,882	16,370	16,697
Loans & advances	40,908	44,800	48,581	52,953	58,248
Fixed Assets	419	528	583	630	680
Other Assets	1,279	1,501	1,598	1,725	1,864
Total Assets	61,808	66,929	69,340	73,593	78,677

Source: Company, KRChoksey Research

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Exhibit 3: Ratio Analysis

Key Ratio	FY17	FY18	FY19	FY20E	FY21E
Growth Rates					
Advances (%)	4.7%	9.5%	8.4%	9.0%	10.0%
Deposits (%)	7.2%	5.9%	5.2%	6.0%	7.0%
Total assets (%)	7.2%	8.3%	3.6%	6.1%	6.9%
NII (%)	16.4%	10.8%	2.8%	6.7%	10.6%
Pre-provisioning profit (%)	20.6%	13.1%	-3.7%	2.4%	7.6%
PAT (%)	6.8%	-43.0%	-39.0%	33.3%	45.9%
B/S Ratios					
Credit/Deposit (%)	76.2%	44.4%	48.6%	50.8%	51.8%
CASA (%)	27.7%	2.1%	2.3%	2.4%	2.5%
Advances/Total assets (%)	66.2%	2.2%	2.3%	2.4%	2.4%
Leverage - Total Assets to Equity	12.27	10.68	10.80	11.50	11.80
Operating efficiency					
Cost/income (%)	45.0%	44.4%	48.6%	50.8%	51.8%
Opex/total assets (%)	2.1%	2.1%	2.3%	2.4%	2.5%
Opex/total interest earning assets	2.1%	2.2%	2.3%	2.4%	2.4%
Profitability					
NIM (%)	3.6%	3.7%	3.5%	3.4%	3.5%
RoA (%)	1.0%	0.5%	0.3%	0.4%	0.5%
RoE (%)	12.5%	5.7%	3.3%	4.2%	5.8%
Asset quality					
Gross NPA (%)	3.6%	6.6%	8.8%	8.6%	8.3%
Net NPA (%)	2.5%	4.2%	5.0%	3.6%	3.5%
PCR (%) (excl. AUCA)	28.9%	36.2%	55.0%	60.0%	60.0%
Slippage (%)	2.5%	3.9%	1.7%	0.8%	0.6%
Credit cost (%)	1.7%	3.0%	3.0%	2.6%	2.3%
Per share data / Valuation					
EPS (INR)	9.95	4.75	2.64	3.52	5.13
BVPS (INR)	82.64	86.21	80.36	86.33	91.53
ABVPS (INR)	65.68	60.57	50.07	62.30	66.17
P/E (x)	7.48	15.65	28.20	21.16	14.51
P/BV (x)	0.90	0.86	0.93	0.86	0.81
P/ABV (x)	1.13	1.23	1.49	1.19	1.12

Source: Company, KRChoksey Research

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Rating Legend (Expected over a 12-month period)	
Our Rating	Upside
Buy	More than 15%
Accumulate	5% – 15%
Hold	0 – 5%
Reduce	-5% – 0
Sell	Less than – 5%

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