

29 June 2020

Karur Vysya Bank

Better placed than other regional banks; maintaining a Buy

Rating: **Buy**

Target Price: ₹49

Share Price: ₹37

Higher margins and lower credit cost led to a sharp ~40% y/y earnings growth for KVB. Asset quality and PCR improved. Given the bank's strong capitalization, coverage and liquidity than its regional peers, it is better placed to withstand Covid'19-related stress. However, with the anticipated slower growth and lower earnings in FY21, we cut our P/ABV multiple to 0.6x (earlier 0.8x), with a lower TP of ₹49 (earlier ₹66).

Better placed than its regional peers. Of the regional banks, KVB with CET-1 at 15.3%, PCR (incl. w/o) at 68.9% and LCR at ~400% is better placed to withstand Covid'19-related stress. ~41% of its current portfolio is under moratorium, with the commercial and corporate portfolios having the highest shares. We have built a base-case scenario, assuming that ~7-8% of customers (weighted average) opting for a moratorium would turn delinquent eventually. We have built in a 3% slippage rate for FY21.

Higher delinquencies to impact the P&L. With an expected higher delinquency rate in H2 FY21, credit cost is expected to be high in the medium term. Higher credit costs combined with weaker operating performance (attributed to slower business growth) would keep the bank's earnings weak in FY21. We estimate -0.7% RoA for FY21 and 1.1% for FY22.

Valuation. Our Jun'21 target of ₹49 is based on the two-stage DDM model. This implies a ~0.5x P/BV and ~0.6x P/ABV multiple on its FY22e book.

Risks: Lumpy slippages from the corporate book; stress in the SME book.

Key financials (YE Mar)	FY18	FY19	FY20	FY21e	FY22e
Net interest income (₹ m)	22,981	23,628	23,479	24,226	27,237
Pre-provisioning profit (₹ m)	17,773	17,108	17,609	17,327	20,525
Provisions (₹ m)	12,737	13,886	14,887	10,282	9,378
PAT (₹ m)	3,457	2,109	2,350	5,269	8,338
EPS (₹)	4.8	2.6	2.9	6.6	10.4
NIM (%)	3.8	3.7	3.6	3.5	3.6
Cost-income (%)	44.4	48.6	49.7	49.9	46.7
RoE (%)	6.1	3.3	3.6	7.8	11.5
RoA (%)	0.5	0.3	0.3	0.7	1.1
Advances growth (%)	9.5	8.4	-5.1	6.0	14.0
GNPA (%)	6.6	8.8	8.7	9.7	7.8
CAR (%)	14.4	16.0	17.2	17.6	17.0
P / E (x)	7.8	14.0	12.6	5.6	3.5
P / BV (x)	0.4	0.5	0.4	0.4	0.4
P / ABV (x)	0.5	0.6	0.6	0.5	0.5

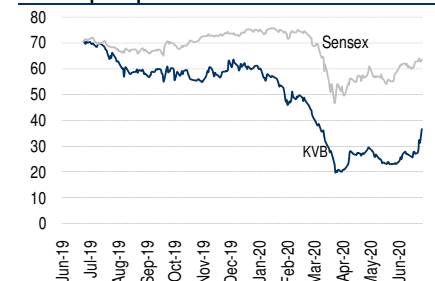
Source: Company, Anand Rathi Research

Key data	KVB IN / KARU.BO
52-week high / low	₹72 / 18
Sensex / Nifty	35171 / 10383
3-m average volume	\$0.7m
Market cap	₹29bn / \$388.5m
Shares outstanding	799m

Shareholding pattern (%)	Mar'20	Dec'19	Sep'19
Promoters	2.1	2.1	2.1
- of which, Pledged	21.8	19.7	20.0
Free float	97.9	97.9	97.9
- Foreign institutions	21.6	20.8	19.6
- Domestic institutions	22.8	23.6	24.3
- Public	53.5	53.5	54.0

Estimates revision (%)	FY21e	FY22e
Net interest income	(9.6)	(10.8)
PAT	(13.0)	(14.1)
RoE	(30.7)	(11.0)

Relative price performance



Source: Bloomberg

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Quick Glance – Financials and Valuations

Fig 1 – Income statement (₹ m)

Year-end: Mar	FY18	FY19	FY20	FY21e	FY22e
Net interest income	22,981	23,628	23,479	24,226	27,237
<i>NII growth (%)</i>	10.8	2.8	-0.6	3.2	12.4
Non-interest income	8,999	9,628	11,546	10,381	11,281
Income	31,980	33,256	35,026	34,607	38,518
<i>Income growth (%)</i>	12.0	4.0	5.3	-1.2	11.3
Operating expenses	14,207	16,148	17,417	17,280	17,993
PPOP	17,773	17,108	17,609	17,327	20,525
<i>PPOP growth (%)</i>	13.1	-3.7	2.9	-1.6	18.5
Provisions	12,737	13,886	14,887	10,282	9,378
PBT	5,036	3,222	2,722	7,045	11,147
Tax	1,580	1,114	372	1,775	2,809
PAT	3,457	2,109	2,350	5,269	8,338
<i>PAT growth (%)</i>	-43.0	-39.0	11.5	124.2	58.2
FDEPS (₹ / sh)	4.8	2.6	2.9	6.6	10.4
DPS (₹ / sh)	0.4	0.1	0.1	2.0	3.1

Source: Company, Anand Rathi Research

Fig 2 – Balance sheet (₹ m)

Year-end: Mar	FY18	FY19	FY20	FY21e	FY22e
Share capital	1,453	1,599	1,599	1,599	1,599
Reserves & surplus	61,189	62,629	64,404	68,093	73,929
Deposits	5,68,901	5,98,680	5,90,751	6,26,196	7,07,601
Borrowings	23,817	15,653	11,842	13,263	14,854
Minority interests	0	0	0	0	0
Total liabilities	6,69,291	6,93,401	6,82,782	7,29,012	8,21,053
Advances	4,48,001	4,85,808	4,60,981	4,88,640	5,57,050
Investments	1,58,032	1,48,816	1,57,624	1,70,234	1,87,258
Cash & bank bal	29,601	29,347	27,327	29,786	32,467
Fixed & other assets	5,282	5,830	5,866	6,160	6,468
Total assets	6,69,291	6,93,401	6,82,782	7,29,012	8,21,053
No. of shares (m)	727	799	799	799	799
<i>Deposits growth (%)</i>	5.9	5.2	-1.3	6.0	13.0
<i>Advances growth (%)</i>	9.5	8.4	-5.1	6.0	14.0

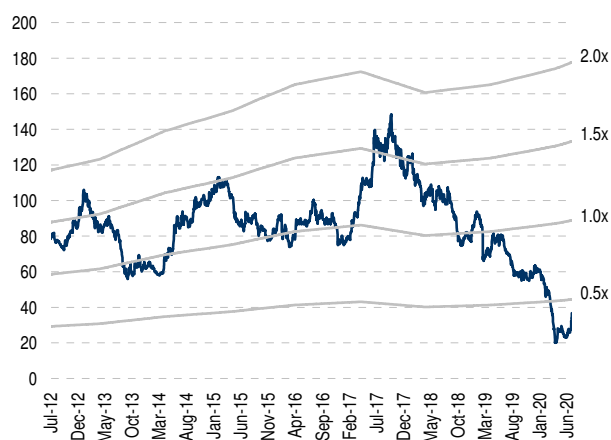
Source: Company, Anand Rathi Research

Fig 3 – Ratio analysis %

Year-end: Mar	FY18	FY19	FY20	FY21e	FY22e
NIM	3.8	3.7	3.6	3.5	3.6
Other inc. / total inc.	28.1	29.0	33.0	30.0	29.3
Cost-income	44.4	48.6	49.7	49.9	46.7
Provision coverage	38.2	45.6	57.1	54.5	62.2
Dividend payout	43.9	19.8	17.8	30.0	30.0
Credit-deposit	78.7	81.1	78.0	78.0	78.7
Investment-deposit	27.8	24.9	26.7	27.2	26.5
Gross NPA	6.6	8.8	8.7	9.7	7.8
Net NPA	4.2	5.0	3.9	4.6	3.1
BV (₹)	86.2	80.4	82.6	87.2	94.5
Adj. BV (₹)	68.3	59.2	66.7	67.4	79.4
CAR	14.4	16.0	17.2	17.6	17.0
- Tier 1	13.9	14.3	15.3	15.7	15.1
RoE	6.1	3.3	3.6	7.8	11.5
RoA	0.5	0.3	0.3	0.7	1.1

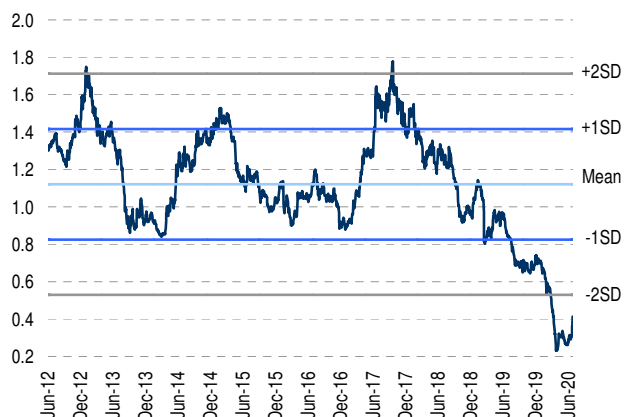
Source: Company, Anand Rathi Research

Fig 4 – Price-to-book band



Source: Bloomberg

Fig 5 – One-year-forward price-to-book value



Source: Company, Anand Rathi Research

Fig 6 – Price movement



Source: Bloomberg

Key Highlights

Fig 7 – Moratorium disclosure (in m)

	Portfolio	Under Moratorium	% Under Moratorium	SMA 0/1/2 under moratorium on 29/2/20
Agri	89,360	22,890	25.6	720
Commercial	1,56,200	89,350	57.2	2190
Corporate	1,27,670	48,800	38.2	350
Retail	1,11,930	37,850	33.8	2720
	4,85,160	1,98,890	41.0	5,980

Source : Company

Fig 8 – Movement of GNPA

GNPA	Q4 FY18	Q1 FY19	Q2 FY19	Q3 FY19	Q4 FY19	Q1 FY20	Q2 FY20	Q3 FY20	Q4 FY20
Opening balance (₹ m)	26,633	30,158	35,634	37,074	40,557	44,496	45,108	43,910	44,240
Slippages (₹ m)	5,890	7,850	1,900	8,880	4,800	4,740	4,170	3,760	3,350
Gross slippage ratio (%)	5.3	6.8	1.6	7.7	4.0	4.0	3.5	3.2	2.9
Reductions (₹ m)	2,366	2,374	466	5,390	860	4,130	5,360	3,440	5,460
Closing balance (₹ m)	30,158	35,634	37,074	40,557	44,496	45,108	43,910	44,240	42,128
GNPA (%)	6.6	7.4	7.7	8.5	8.8	9.2	8.9	8.9	8.7
Restructured advances (%)	0.6	0.1	0.1	0.2	0.1	0.3	0.3	0.4	0.4
Stressed assets (%)	7.1	7.5	7.8	8.6	8.9	9.5	9.2	9.4	9.1

Source: Company, Anand Rathi Research

Fig 9 – Break-up of advances (%)

	Q1 FY19	Q2 FY19	Q3 FY19	Q4 FY19	Q1 FY20	Q2 FY20	Q3 FY20	Q4 FY20
Corporate	31.1	30.0	28.3	28.0	27.6	26.9	26.4	26.3
Commercial	34.5	34.4	35.1	33.7	33.6	32.6	32.7	32.2
Retail	17.2	18.4	19.3	22.3	22.1	23.8	23.7	23.1
Housing	6.2	6.6	7.1	7.1	7.9	8.4	8.8	9.4
Auto	2.2	2.2	2.2	2.1	2.1	2.1	2.1	2.0
Education	0.5	0.5	0.5	0.5	0.5	0.5	0.4	0.4
Personal	0.6	0.7	0.8	0.8	0.9	1.0	1.1	1.2
Jewel	1.2	1.2	1.2	1.2	1.3	1.4	1.5	1.8
LAP	3.1	3.3	3.4	3.4	3.5	3.7	3.5	3.5
Other retail	3.3	3.9	4.0	7.1	5.9	6.8	6.3	4.8
Farm	17.2	17.2	17.3	16.0	16.6	16.7	17.2	18.4
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: Company, Anand Rathi Research

Quarterly snapshot

Fig 10 – Income statement

(₹ m)	Q2 FY18	Q3 FY18	Q4 FY18	Q1 FY19	Q2 FY19	Q3 FY19	Q4 FY19	Q1 FY20	Q2 FY20	Q3 FY20	Q4 FY20
Interest income	14,024	14,223	14,909	14,425	14,569	14,428	14,736	14,925	15,375	15,038	14,562
Interest expense	8,474	8,607	8,480	8,589	8,778	8,619	8,544	9,086	9,412	9,266	8,657
NII	5,550	5,616	6,429	5,836	5,791	5,808	6,192	5,840	5,963	5,772	5,905
Y/Y growth %	12.1	8.5	10.8	8.4	4.3	3.4	(3.7)	0.1	3.0	(0.6)	(4.6)
Non-interest income	2,301	2,249	2,087	2,549	1,756	2,599	2,725	2,698	2,777	2,601	3,470
Trading profits	200	260	80	70	(210)	270	570	670	910	450	1,370
Total income	7,851	7,865	8,515	8,385	7,547	8,407	8,917	8,538	8,740	8,373	9,375
Y/Y growth %	10.1	14.4	4.9	8.2	(3.9)	6.9	4.7	1.8	15.8	(0.4)	5.1
Operating expenses	3,581	3,653	3,718	3,789	3,933	4,157	4,269	4,087	4,429	4,525	4,376
Of which, staff cost	1,551	1,534	1,792	1,786	1,727	1,977	2,123	2,038	2,130	2,255	2,144
PPOP	4,270	4,212	4,797	4,596	3,614	4,250	4,648	4,451	4,312	3,847	4,998
Y/Y growth %	33.6	55.0	(5.4)	2.3	(15.4)	0.9	(3.1)	(3.2)	19.3	(9.5)	7.5
Total provisions	3,214	3,247	3,942	4,227	2,131	4,004	3,523	3,300	3,652	3,643	4,293
PBT	1,057	965	855	370	1,483	246	1,124	1,152	660	205	706
Tax	300	250	350	(90)	645	34	524	422	27	54	(131)
PAT	756	715	506	459	837	212	600	729	633	151	837
Y/Y growth %	(40.1)	(38.2)	(76.8)	(69.0)	10.7	(70.3)	18.7	58.8	(24.4)	(28.9)	39.5

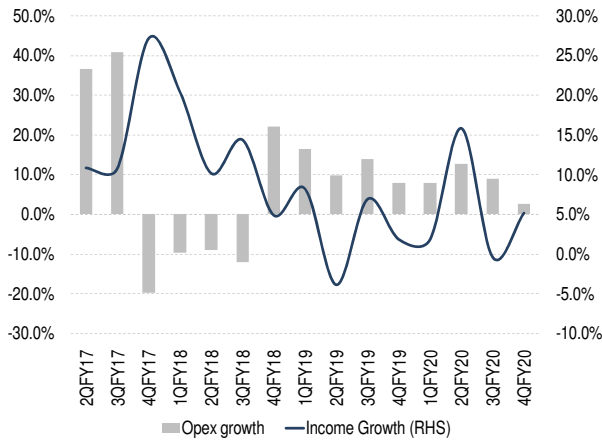
Source: Company, Anand Rathi Research

Fig 11 – Balance sheet

(₹ m)	Q2 FY18	Q3 FY18	Q4 FY18	Q1 FY19	Q2 FY19	Q3 FY19	Q4 FY19	Q1 FY20	Q2 FY20	Q3 FY20	Q4 FY20
Equity capital	1,219	1,450	1,453	1,453	1,599	1,600	1,599	1,600	1,599	1,599	1,599
Reserves & Surplus	51,319	60,680	61,189	61,647	61,814	62,030	62,629	63,360	63,414	63,565	64,404
Deposits	5,63,999	5,71,200	5,68,901	5,75,540	5,82,618	5,86,240	5,98,680	6,17,110	6,22,128	6,22,620	5,90,751
Borrowings	6,630	17,370	23,817	30,750	18,843	9,590	15,653	27,050	30,527	-	11,842
Other Liabilities	16,422	14,610	13,932	13,370	14,331	16,440	14,840	15,030	16,475	-	14,186
Total Equity and Liabilities	6,39,587	6,65,310	6,69,291	6,82,760	6,79,204	6,75,900	6,93,401	7,24,150	7,34,143	6,87,784	6,82,782
Deposits y/y growth %	8.5	3.7	5.9	5.3	3.3	2.6	5.2	7.2	6.8	6.2	(1.3)
Deposits q/q growth %	3.2	1.3	(0.4)	1.2	1.2	0.6	2.1	3.1	0.8	0.1	(5.1)
Assets											
Cash and cash balances	39,379	41,630	42,969	38,400	40,275	32,210	36,970	61,430	54,210	-	43,926
Advances	4,34,348	4,37,920	4,48,002	4,64,060	4,64,798	4,60,050	4,85,808	4,69,820	4,71,018	4,71,190	4,60,981
Investments	1,46,804	1,65,970	1,58,032	1,61,080	1,55,371	1,62,050	1,48,816	1,69,830	1,83,984	-	1,57,624
Other assets	19,056	19,790	20,289	19,220	18,760	21,590	21,807	23,070	24,932	-	20,251
Total Assets	6,39,587	6,65,310	6,69,291	6,82,760	6,79,204	6,75,900	6,93,401	7,24,150	7,34,143	4,71,190	6,82,782
Advances y/y growth %	11.0	13.9	9.5	11.3	7.0	5.1	8.4	1.2	1.3	2.4	(5.1)
Advances q/q growth %	4.2	0.8	2.3	3.6	0.2	(1.0)	5.6	(3.3)	0.3	0.0	(2.2)

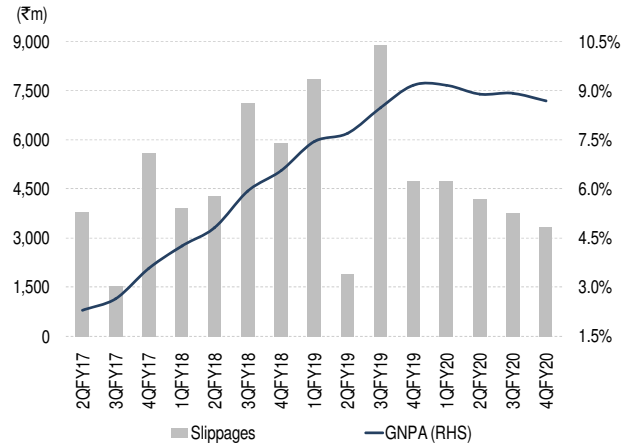
Source: Company, Anand Rathi Research

Fig 12 – Income vs. Opex growth



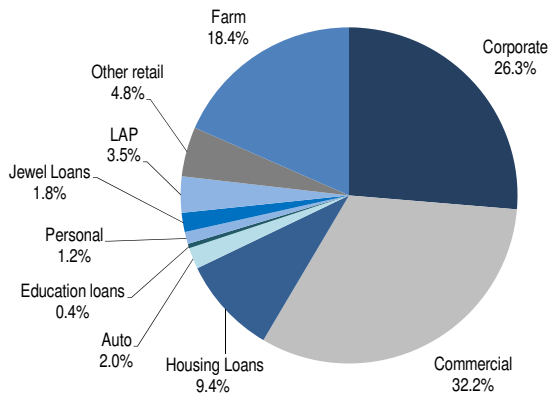
Source: Company, Anand Rathi Research

Fig 13 – Gross NPA and slippages



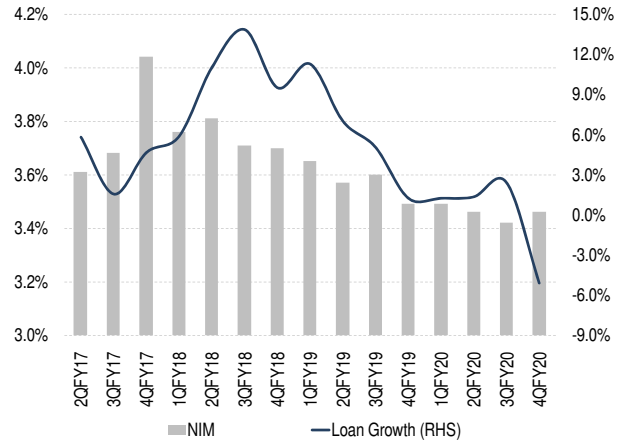
Source: Company, Anand Rathi Research

Fig 14 – Loan break-up



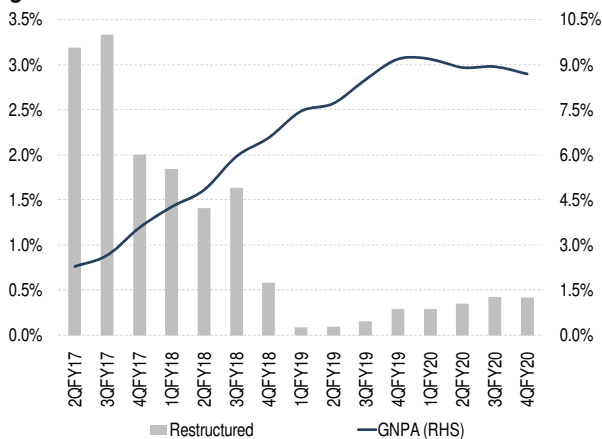
Source: Company, Anand Rathi Research

Fig 15 – Credit growth vs. NIM



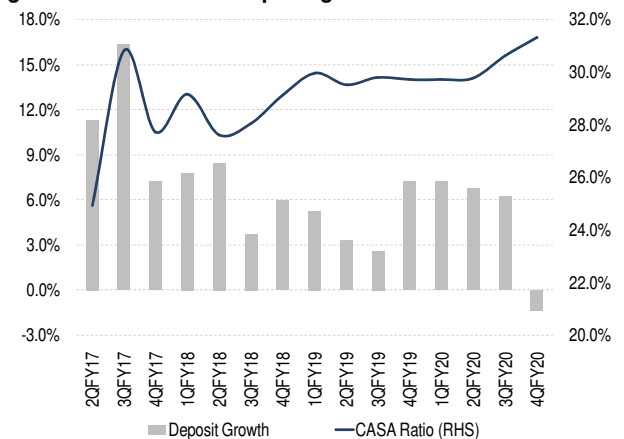
Source: Company, Anand Rathi Research

Fig 16 – Restructured assets vs. GNPA



Source: Company, Anand Rathi Research

Fig 17 – CASA ratio vs. Deposit growth



Source: Company, Anand Rathi Research

Valuation

Our Jun'21 target of ₹49 is based on the two-stage DDM model. This implies a ~0.5x P/BV and ~0.6x P/ABV multiple on its FY22e book.

We are positive about the bank's loan growth potential, largely driven by its retail and commercial books.

Fig 18 – Change in estimates

	FY21e			FY22e		
	New	Old	Chg %	New	Old	Chg %
Net Interest Income (₹ m)	24,226	26,810	(9.6)	27,237	30,532	(10.8)
PAT (₹ m)	17,327	19,927	(13.0)	20,525	23,885	(14.1)
RoE (%)	7.8	11.2	(30.7)	11.5	12.9	(11.0)

Source: Anand Rathi Research

Risks

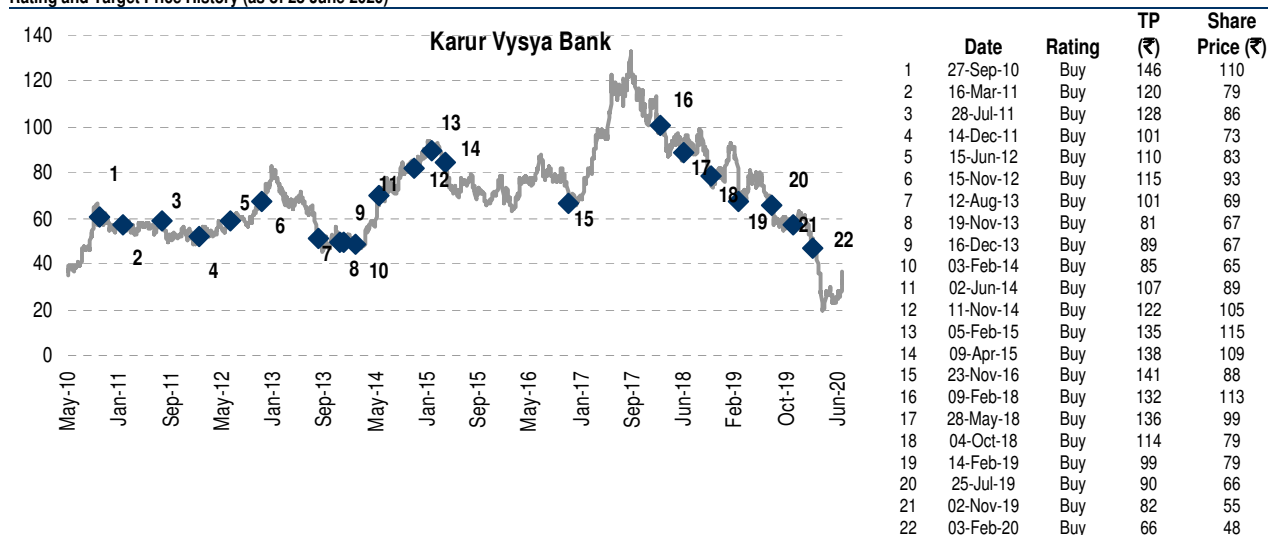
- Higher slippages in future (especially from the corporate portfolio) could lead to volatility in asset quality.
- Stress in the SME book.

Appendix

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	Buy	Hold	Sell
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