

3 August 2020

Karur Vysya Bank

Decent quarter, asset quality stable; maintaining a Buy

Rating: **Buy**

Target Price: ₹49

Share Price: ₹35

Higher Treasury income, lower opex and lower credit cost led to steep, ~45% y/y, earnings growth for KVB. Its asset quality and PCR improved. With ~41% of its portfolio under moratorium, asset quality may come under stress once the moratorium is lifted, keeping FY21 earnings muted. Given the bank's strong capitalization, coverage and liquidity compared to its regional peers, it is better placed to withstand Covid'19-related stress. We maintain a Buy with a TP of ₹49.

H2 FY21 asset quality may be stressed. ~42% of KVB's portfolio (by value) is under moratorium. Most, though, is adequately collateral-ized; nevertheless, given the weak economic milieu, the delinquency rate is expected to sharply rise once the moratorium is lifted. On a base case scenario, we've assumed that 10%-12% of customers opting for a moratorium would eventually turn delinquent. We have built in a 4% slippage rate for FY21.

Slower business, higher delinquencies to impact the P&L. Given the weak economic outlook, we expect the bank's loan growth to be in single digits in FY21. Slower business growth would lead to lower NII and fee income. A weak operating performance combined with higher credit cost would keep FY21 earnings muted. We estimate 0.7% RoA for FY21 and 1.1% for FY22.

Valuation. Our Jul'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.

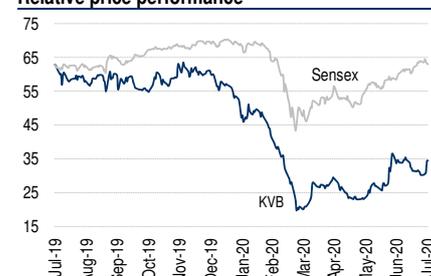
Key financials (YE Mar)	FY18	FY19	FY20	FY21e	FY22e
Net interest income (₹ m)	22,981	23,628	23,479	24,226	27,237
Pre-provisioning profit (₹ m)	17,773	17,108	17,609	17,327	20,525
Provisions (₹ m)	12,737	13,886	14,887	10,282	9,378
PAT (₹ m)	3,457	2,109	2,350	5,269	8,338
EPS (₹)	4.8	2.6	2.9	6.6	10.4
NIM (%)	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)	7.3	13.2	11.9	5.3	3.4
P / BV (x)	0.4	0.4	0.4	0.4	0.4
P / ABV (x)	0.5	0.6	0.5	0.5	0.4

Source: Company, Anand Rathi Research

Key data	KVB IN / KARU.BO
52-week high / low	₹65 / 18
Sensex / Nifty	37607 / 11073
3-m average volume	\$1.1m
Market cap	₹28bn / \$370.8m
Shares outstanding	799m

Shareholding pattern (%)	Jun'20	Mar'20	Dec'19
Promoters	2.1	2.1	2.1
- of which, Pledged	21.6	21.8	19.7
Free float	97.9	97.9	97.9
- Foreign institutions	21.1	21.6	20.8
- Domestic institutions	22.2	22.8	23.6
- Public	54.7	53.5	53.5

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)

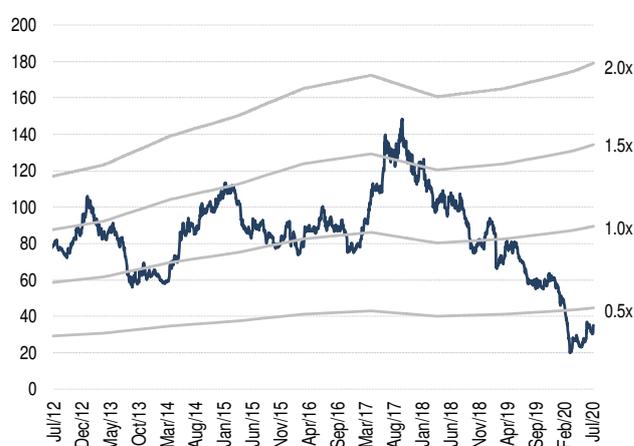
Year-end: Mar	FY18	FY19	FY20	FY21e	FY22e
Share capital	1,453	1,599	1,599	1,599	1,599
Reserves & surplus	61,189	62,629	64,404	68,093	73,929
Deposits	568,901	598,680	590,751	626,196	707,601
Borrowings	23,817	15,653	11,842	13,263	14,854
Minority interests	0	0	0	0	0
Total liabilities	669,291	693,401	682,782	729,012	821,053
Advances	448,001	485,808	460,981	488,640	557,050
Investments	158,032	148,816	157,624	170,234	187,258
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	669,291	693,401	682,782	729,012	821,053
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

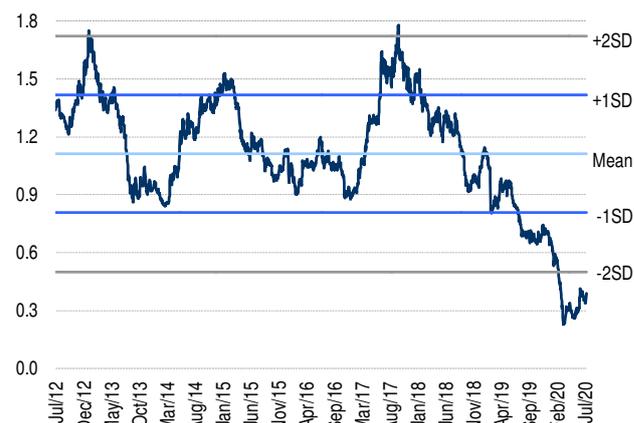
Fig 3 – Ratio analysis %

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

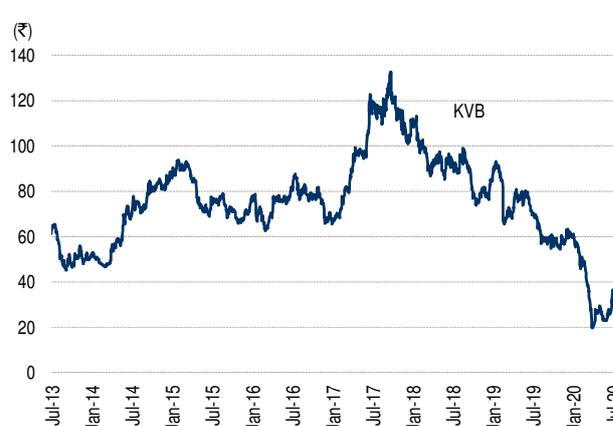
Source: Company, Anand Rathi Research

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

Conference-call takeaways

Moratorium

- 41% of the bank's portfolio is under moratorium. Excluding gold loans, the portfolio is 37%.
- Of this moratorium book, 48% is of term loans; 47%, working-capital loans.
- **Term loans.** Of the ₹86.3bn portfolio under moratorium in this category:
 - 34% of the customers have not paid a single EMI.
 - 49% have paid one EMI.
 - 10% have paid two EMIs.
 - 2% have paid three EMIs.
 - 3% have paid four EMIs.
 - 1% of the customers have pre-paid.
- **Working capital loans.** Of this portfolio, 10%-15% of the accounts has seen no transitions. Management said this could be due to access issues.
- ₹8.89bn are accounts under standstill, on which the bank has made a provision of ₹1.2bn.
- Under a stress test, even in the worst case, the capital adequacy of the bank would be well above the regulatory levels.

Others

- Under the government-guaranteed MSME scheme, of the eligible ₹27.6bn, the bank has disbursed ₹7.75bn.
- It expects credit cost of between 1.5% and 2% in FY21. In the worst case, this could go to 2.5%.
- On the investment book, the bank has deployed ₹70bn in short-term instruments to mitigate the risk.
- Management expects NIM to remain at the current levels.

Fig 7 – Movement of GNPA

GNPA	Q1 FY19	Q2 FY19	Q3 FY19	Q4 FY19	Q1 FY20	Q2 FY20	Q3 FY20	Q4 FY20	Q1 FY21
Opening balance (₹ m)	30,158	35,634	37,074	40,557	44,496	45,108	43,910	44,240	42,128
Slippages (₹ m)	7,850	1,900	8,880	4,800	4,740	4,170	3,760	3,350	400
Gross slippage ratio (%)	6.8	1.6	7.7	4.0	4.0	3.5	3.2	2.9	0.3
Reductions (₹ m)	2,374	466	5,390	860	4,130	5,360	3,440	5,460	1,980
Closing balance (₹ m)	35,634	37,074	40,557	44,496	45,108	43,910	44,240	42,128	40,557
GNPA (%)	7.4	7.7	8.5	8.8	9.2	8.9	8.9	8.7	8.3
Restructured advances (%)	0.1	0.1	0.2	0.1	0.3	0.3	0.4	0.4	0.4
Stressed assets (%)	7.5	7.8	8.6	8.9	9.5	9.2	9.4	9.1	8.8

Source: Company, Anand Rathi Research

Fig 8 – Break-up of advances (%)

	Q2 FY19	Q3 FY19	Q4 FY19	Q1 FY20	Q2 FY20	Q3 FY20	Q4 FY20	Q1 FY21
Corporate	30.0	28.3	28.0	27.6	26.9	26.4	26.3	24.6
Commercial	34.4	35.1	33.7	33.6	32.6	32.7	32.2	33.1
Retail	18.4	19.3	22.3	22.1	23.8	23.7	23.1	22.5
Housing	6.6	7.1	7.1	7.9	8.4	8.8	9.4	9.5
Auto	2.2	2.2	2.1	2.1	2.1	2.1	2.0	2.0
Education	0.5	0.5	0.5	0.5	0.5	0.4	0.4	0.4
Personal	0.7	0.8	0.8	0.9	1.0	1.1	1.2	1.1
Jewel	1.2	1.2	1.2	1.3	1.4	1.5	1.8	2.1
LAP	3.3	3.4	3.4	3.5	3.7	3.5	3.5	3.4
Other retail	3.9	4.0	7.1	5.9	6.8	6.3	4.8	4.0
Farm	17.2	17.3	16.0	16.6	16.7	17.2	18.4	19.8
Total	100.0							

Source: Company, Anand Rathi Research

Quarterly snapshot

Fig 9 – Income statement

(₹ m)	Q3 FY18	Q4 FY18	Q1 FY19	Q2 FY19	Q3 FY19	Q4 FY19	Q1 FY20	Q2 FY20	Q3 FY20	Q4 FY20	Q1 FY21
Interest income	14,223	14,909	14,425	14,569	14,428	14,736	14,925	15,375	15,038	14,562	13,761
Interest expense	8,607	8,480	8,589	8,778	8,619	8,544	9,086	9,412	9,266	8,657	8,143
NII	5,616	6,429	5,836	5,791	5,808	6,192	5,840	5,963	5,772	5,905	5,618
Y/Y growth %	8.5	10.8	8.4	4.3	3.4	(3.7)	0.1	3.0	(0.6)	(4.6)	(3.8)
Non-interest income	2,249	2,087	2,549	1,756	2,599	2,725	2,698	2,777	2,601	3,470	3,171
Trading profits	260	80	70	(210)	270	570	670	910	450	1,370	1,780
Total income	7,865	8,515	8,385	7,547	8,407	8,917	8,538	8,740	8,373	9,375	8,790
Y/Y growth %	14.4	4.9	8.2	(3.9)	6.9	4.7	1.8	15.8	(0.4)	5.1	2.9
Operating expenses	3,653	3,718	3,789	3,933	4,157	4,269	4,087	4,429	4,525	4,376	4,051
Of which, staff cost	1,534	1,792	1,786	1,727	1,977	2,123	2,038	2,130	2,255	2,144	2,136
PPOP	4,212	4,797	4,596	3,614	4,250	4,648	4,451	4,312	3,847	4,998	4,739
Y/Y growth %	55.0	(5.4)	2.3	(15.4)	0.9	(3.1)	(3.2)	19.3	(9.5)	7.5	6.5
Total provisions	3,247	3,942	4,227	2,131	4,004	3,523	3,300	3,652	3,643	4,293	3,376
PBT	965	855	370	1,483	246	1,124	1,152	660	205	706	1,363
Tax	250	350	(90)	645	34	524	422	27	54	(131)	308
PAT	715	506	459	837	212	600	729	633	151	837	1,055
Y/Y growth %	(38.2)	(76.8)	(69.0)	10.7	(70.3)	18.7	58.8	(24.4)	(28.9)	39.5	44.7

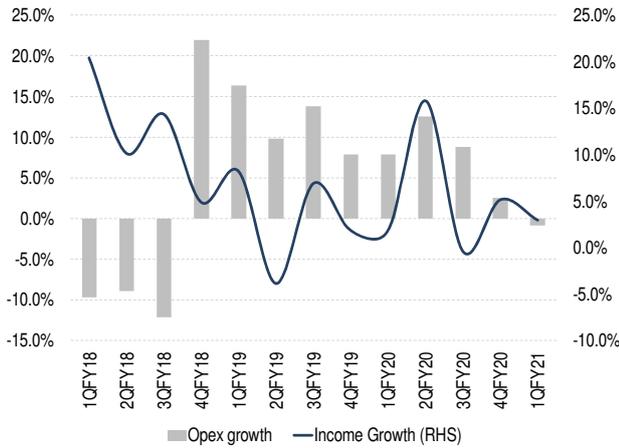
Source: Company, Anand Rathi Research

Fig 10 – Balance sheet

(₹ m)	Q3 FY18	Q4 FY18	Q1 FY19	Q2 FY19	Q3 FY19	Q4 FY19	Q1 FY20	Q2 FY20	Q3 FY20	Q4 FY20	Q1 FY21
Equity capital	1,450	1,453	1,453	1,599	1,600	1,599	1,600	1,599	1,599	1,599	1,600
Reserves & Surplus	60,680	61,189	61,647	61,814	62,030	62,629	63,360	63,414	63,565	64,404	65,460
Deposits	571,200	568,901	575,540	582,618	586,240	598,680	617,110	622,128	622,620	590,751	600,650
Borrowings	17,370	23,817	30,750	18,843	9,590	15,653	27,050	30,527	-	11,842	10,410
Other Liabilities	14,610	13,932	13,370	14,331	16,440	14,840	15,030	16,475	-	14,186	15,680
Total Equity and Liabilities	665,310	669,291	682,760	679,204	675,900	693,401	724,150	734,143	687,784	682,782	693,800
Deposits y/y growth %	3.7	5.9	5.3	3.3	2.6	5.2	7.2	6.8	6.2	(1.3)	(2.7)
Deposits q/q growth %	1.3	(0.4)	1.2	1.2	0.6	2.1	3.1	0.8	0.1	(5.1)	1.7
Assets											
Cash and cash balances	41,630	42,969	38,400	40,275	32,210	36,970	61,430	54,210	-	43,926	41,760
Advances	437,920	448,002	464,060	464,798	460,050	485,808	469,820	471,018	471,190	460,981	461,310
Investments	165,970	158,032	161,080	155,371	162,050	148,816	169,830	183,984	-	157,624	170,330
Other assets	19,790	20,289	19,220	18,760	21,590	21,807	23,070	24,932	-	20,251	20,400
Total Assets	665,310	669,291	682,760	679,204	675,900	693,401	724,150	734,143	471,190	682,782	693,800
Advances y/y growth %	13.9	9.5	11.3	7.0	5.1	8.4	1.2	1.3	2.4	(5.1)	(1.8)
Advances q/q growth %	0.8	2.3	3.6	0.2	(1.0)	5.6	(3.3)	0.3	0.0	(2.2)	0.1

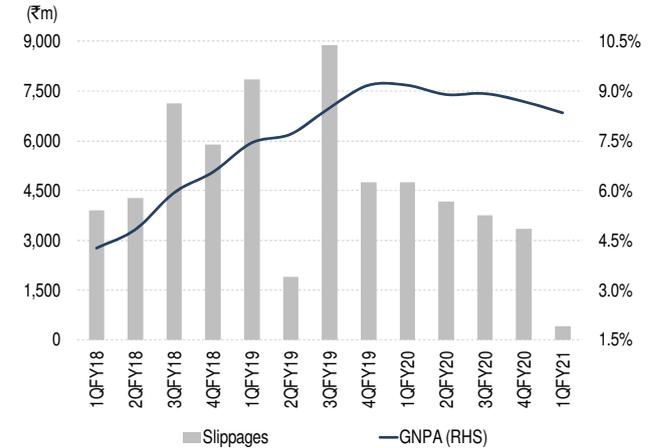
Source: Company, Anand Rathi Research

Fig 11 – Income vs. Opex growth



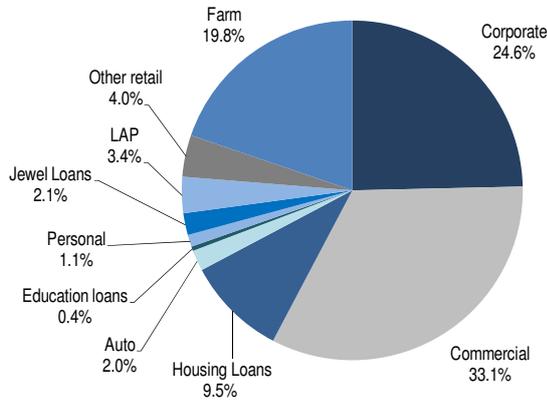
Source: Company, Anand Rathi Research

Fig 12 – Gross NPA and slippages



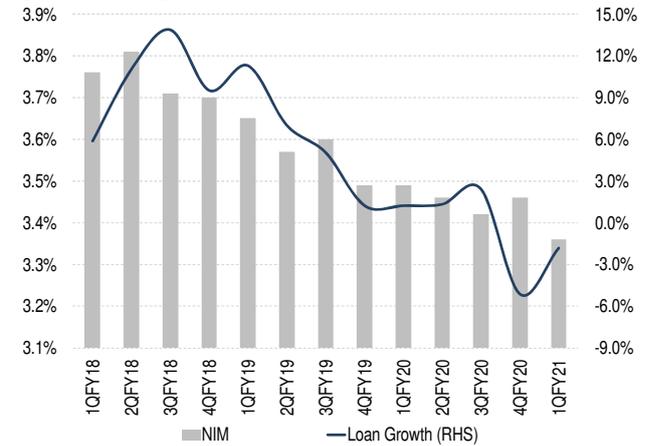
Source: Company, Anand Rathi Research

Fig 13 – Loan break-up



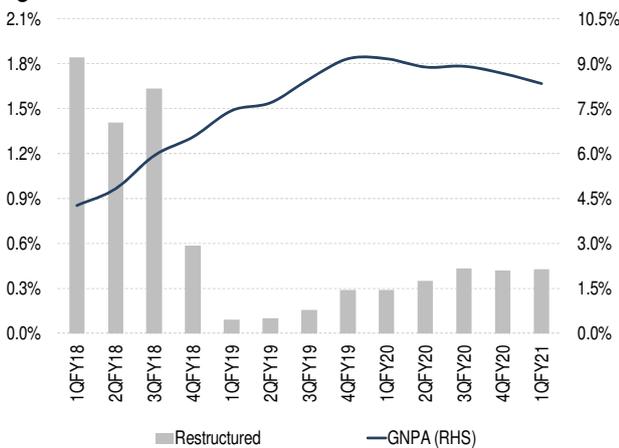
Source: Company, Anand Rathi Research

Fig 14 – Credit growth vs. NIM



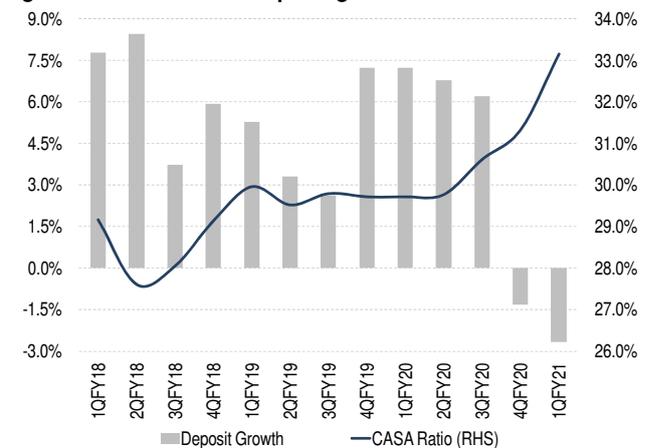
Source: Company, Anand Rathi Research

Fig 15 – Restructured assets vs. GNPA



Source: Company, Anand Rathi Research

Fig 16 – CASA ratio vs. Deposit growth



Source: Company, Anand Rathi Research

Fig 17 – Moratorium disclosure

(₹m)	Portfolio (as on 30th June)	Under Moratorium (as on 31st Mar)	Under Moratorium (as on 24th July)	Under Moratorium excl gold loans (as on 24th July)
Agri	96,090	31%	19%	4%
Commercial	160,740	79%	55%	55%
Corporate	119,780	40%	44%	44%
Retail	109,560	43%	35%	35%
	486,170	52%	41%	37%

Source: Company

Valuation

Our Jul'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.

Risks

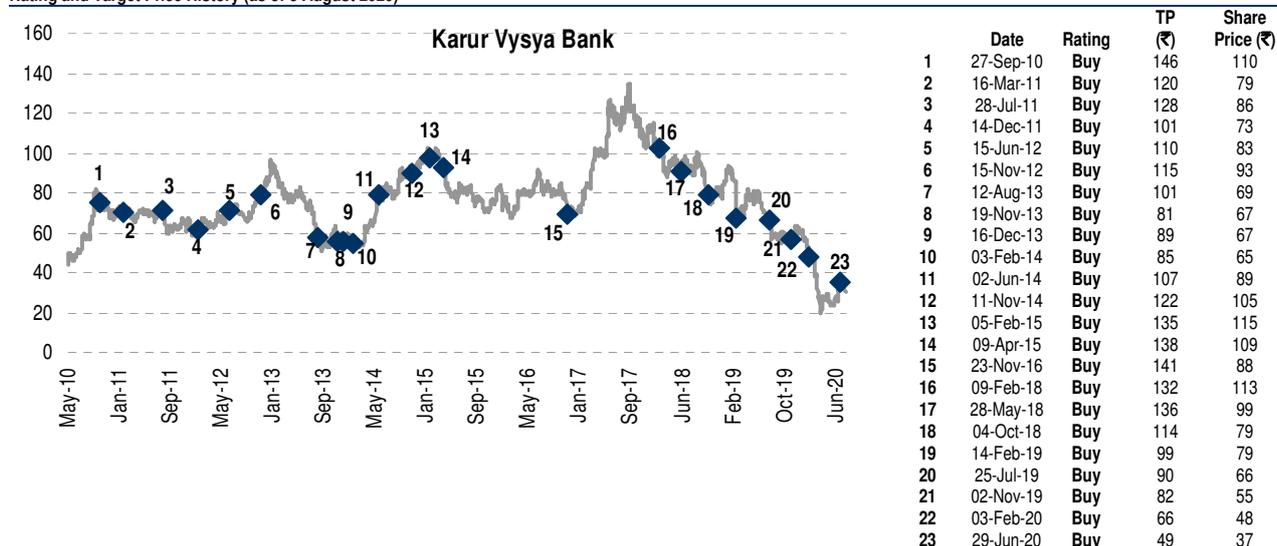
- Higher slippages in future (especially from the corporate portfolio) could lead to volatility in asset quality.
- Stress in the SME book.

Appendix

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	Buy	Hold	Sell
Large Caps (>US\$1bn)	>15%	5-15%	<5%
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