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Karur Vysya Bank

Higher margins, NPA recovery fuel ROA to a decadal high

CMP	Target Price
Rs 109 as of (January 23, 2023)	Rs 155 (▲) 12 months
Rating	**Upside**
BUY (■)	42.9 %

- Despite higher provisions including hit on SR book, KVB reported a 13% beat on PAT at Rs2.9bn (vs est: Rs2.6bn), mainly due to continued margin expansion, recovery from written-off accounts (Rs0.85bn) and lower effective tax rate (due to higher w-offs). As promised, the bank has brought down NNPA below 1% (to 0.9%), and expects incremental LLP to be lower; it thereby guides for exit RoA of 1.35% in 4Q (1.3% in 3Q).
- Overall gross credit growth was healthy at 16% YoY/4% QoQ, while net credit growth at 16% YoY/3% QoQ was due to higher w-offs. However, higher asset re-pricing of the MCLR portfolio led to 25bps QoQ improvement in NIMs at 4.3%. Bank has started the pilot run for its MFI business via BC tie-up, sensing a high-margin business opportunity and a granularized portfolio.
- The Board has extended MD & CEO Ramesh Babu's term (ending on July 29, 2023) for another 3 years, subject to approval by the RBI; this is comforting, given his contribution in the current transformational journey of the bank. We raise our FY23/24/25 earnings estimates by 6%/2%/4%, mainly driven by better NIMs and lower opex & LLP.
- KVB remains one of our top picks in the small banking space, given expected improvement in its RoA/RoE to a decadal high of 1.4%/16%, healthy capital ratios and emerging Management credibility. We retain BUY, with a revised TP of Rs155, up from Rs125, and now value the bank at 1.2x Dec-24E ABV (vs earlier 1x Sep-24E ABV earlier).

Margins shoot up, led by healthy growth/asset re-pricing: Overall gross credit growth was healthy at 16% YoY/4% QoQ due to strong corporate & retail growth, while SME book growth slowed down a bit. Bank's retail growth was mainly driven by mortgages/LAP and gold loans; the bank has now entered into tie-ups with BCs to launch its MFI business. This is mainly to diversify growth vectors without compromising on margins and also to avoid dependence on lumpy, consortium-based corporate loans, as in the past. Deposits growth was decent at 14% YoY/3% QoQ, due to faster growth in TDs; as a result, CASA ratio declined to 34%. However, higher asset re-pricing of its MCLR portfolio led to a 25-bps QoQ improvement in NIMs at 4.3%. Bank expects NIM to remain above 4%, given the changing loan composition and better asset-liability management.

NPAs continue to trend down due to negative net slippages and accelerated w-offs: Fresh slippages were lower than expected at Rs1.6bn/1.2% of loans, which coupled with better recovery and accelerated write-offs, led to a sharp 1.3% reduction in GNPA ratio to 2.7%/NNPA to 0.9%. Bank expects continued net negative slippages, which should thus keep GNPA below 2.5%. The restructured pool too declined, to 1.9% of loans from 2% in Q2. With the heavy lifting on PCR improvement largely behind, Bank targets LLP at below 1% in FY24E.

Outlook and valuations: KVB remains one of our top picks in the small banking space, given the expected improvement in its RoA/RoE to a decadal high of 1.4%/16%, healthy capital ratios and emerging Management credibility. We retain BUY with a revised TP of Rs155/share, up from Rs125, and now value the bank at 1.2x Dec-24E ABV (vs earlier 1x Sep-24E ABV earlier). **Key risks**: Slower than expected growth, faster decline in CASA leading to cost pressure, and resurgence of NPAs in the retail/SME sector due to macro dislocation.

Change in Estimates	
EPS Chg FY23E/FY24E (%)	6.0/1.5
Target Price change (%)	24.0
Target Period (Months)	12
Previous Reco	BUY

Emkay vs Consensus		
EPS Estimates		
	FY23E	FY24E
Emkay	13.3	16.5
Consensus	12.3	15.3
Mean Consensus TP (12M)		Rs 122

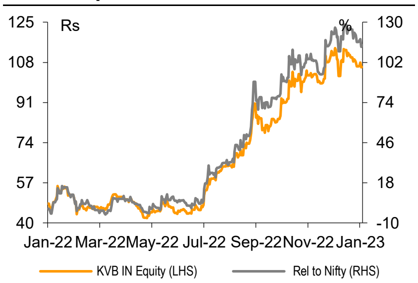
Stock Details	
Bloomberg Code	KVB IN
Face Value (Rs)	2
Shares outstanding (mn)	799
52 Week H/L	116 / 42
M Cap (Rs bn/USD bn)	87 / 1.07
Daily Avg Volume (nos.)	6,899,754
Daily Avg Turnover (USD mn)	8.8

Shareholding Pattern Sep '22	
Promoters	2.3%
FIIs	16.5%
DIIs	25.2%
Public and Others	56.1%

Price Performance

(%)	1M	3M	6M	12M
Absolute	6	19	101	125
Rel. to Nifty	4	16	86	119

Relative price trend



Source: Bloomberg

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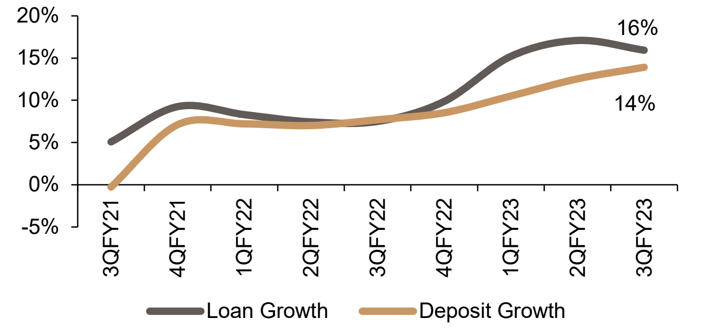
Financial Snapshot (Standalone)

(Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
Net income	32,783	34,844	43,277	49,636	58,167
Net profit	3,594	6,733	10,610	13,240	16,337
EPS (Rs)	4.5	8.4	13.3	16.5	20.4
ABV (Rs)	71.0	83.2	102.4	116.7	134.1
RoA (%)	0.5	0.9	1.2	1.3	1.4
RoE (%)	5.3	9.3	13.2	14.6	15.8
P/E (x)	24.1	12.9	8.2	6.6	5.3
P/ABV	1.5	1.3	1.1	0.9	0.8

Source: Company, Emkay Research

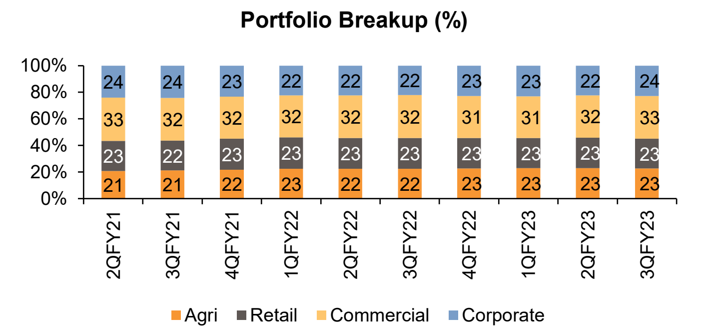
Story in charts

Exhibit 1: Overall gross credit growth was healthy at 16% yoy/4% qoq due to strong corporate and retail growth



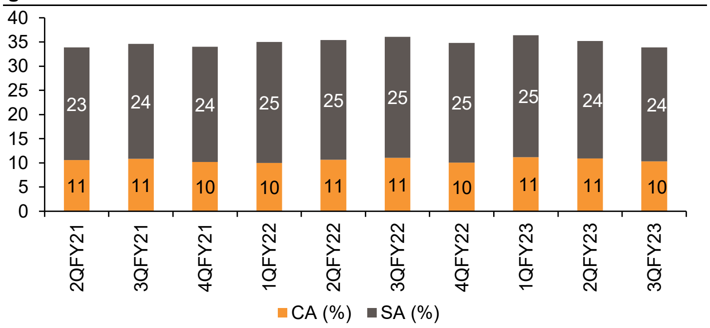
Source: Company, Emkay Research

Exhibit 2: Bank has a relatively well balanced portfolio



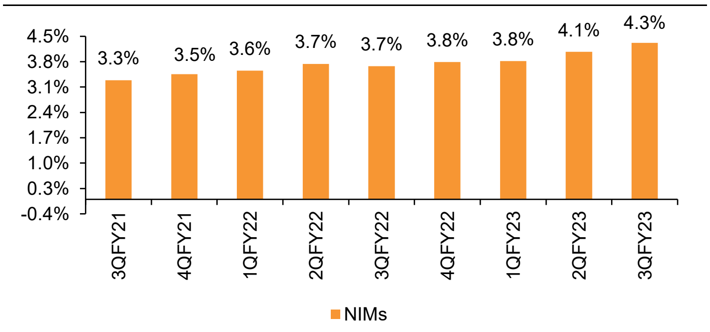
Source: Company, Emkay Research

Exhibit 3: CASA ratio moderated by 133bps to 34%, owing to faster growth in TDs



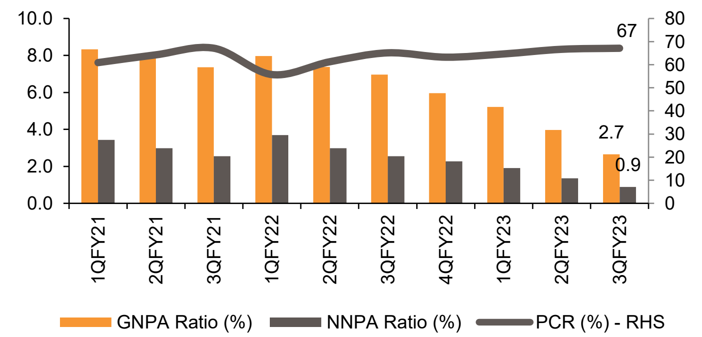
Source: Company, Emkay Research

Exhibit 4: …but asset repricing led to 25bps qoq improvement in NIMs to 4.3%



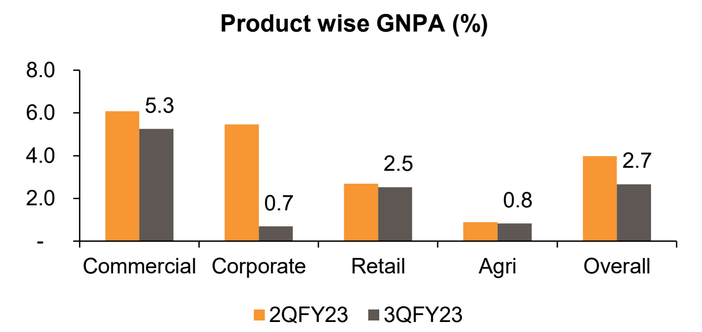
Source: Company, Emkay Research

Exhibit 5: Negative net slippages + higher w-offs led to NNPA falling below 1%



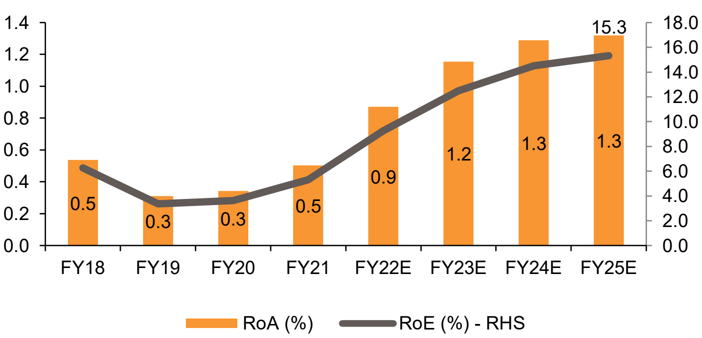
Source: Company, Emkay Research

Exhibit 6: Corporate and Commercial stress is now behind, leading to improvement in segmental NPAs



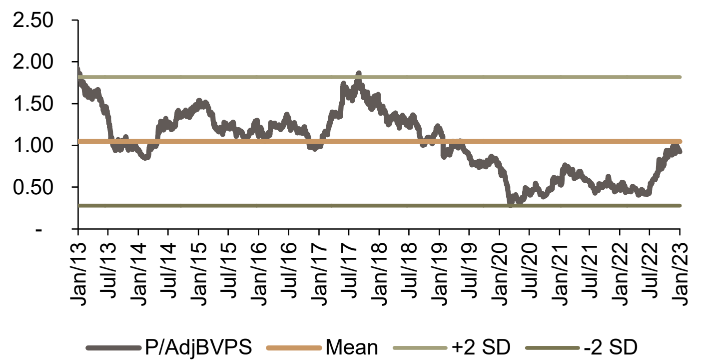
Source: Company, Emkay Research

Exhibit 7: We expect steady growth in return ratios, led by better growth and lower LLP



Source: Company, Emkay Research

Exhibit 8: The stock currently trades at 0.9x one-year forward ABV



Source: Bloomberg, Emkay Research

Exhibit 9: Actuals vs. Estimates (Q3FY23)

Rs mn	Actuals	Estimates		Variation		Comments
		Emkay	Consensus	Emkay	Consensus	
Net income	12,065	10,461	10,489	15%	15%	Better margins and higher other income led to a beat
PPOP	6,890	5,243	5,730	31%	20%	Higher Net income and in-line opex led to a beat
PAT	2,893	2,556	2,663	13%	9%	Higher PPOP and Lower tax, partly offset by higher LLP, led to a beat

Source: Company, Emkay Research

Exhibit 10: Quarterly Summary

(Rs mn)	1QFY22	2QFY22	3QFY22	4QFY22	1QFY23	2QFY23	3QFY23	YoY (%)	QoQ (%)	FY22	FY23E	YoY (%)
Interest Earned	13,759	13,980	14,045	14,093	14,735	15,795	16,952	21	7	55,877	65,440	17
Interest Exp	7,380	7,176	7,173	6,993	7,277	7,581	8,062	12	6	28,723	32,125	12
Net Interest Income	6,379	6,803	6,872	7,099	7,459	8,214	8,890	29	8	27,154	33,315	23
Global NIMs (reported)	3.55	3.74	3.68	3.79	3.82	4.07	4.32	64bps	25bps	3.69	4.05	36bps
Non-interest Income	2,010	1,631	1,956	2,055	1,991	2,416	3,175	62	31	7,691	9,962	30
Operating Expenses	4,293	4,696	4,813	4,741	4,695	4,906	5,175	8	5	18,542	20,248	9
Pre Provisioning Profit	4,096	3,738	4,016	4,413	4,755	5,723	6,890	72	20	16,302	23,029	41
Provision & Contingencies	2,450	1,642	1,461	1,401	1,546	2,272	3,641	149	60	6,993	9,427	35
PBT	1,646	2,097	2,555	3,012	3,208	3,451	3,249	27	-6	9,309	13,602	46
Income Tax Expense (Gain)	557	442	700	877	921	949	356	-49	-63	2,577	2,992	16
Net Profit/(Loss)	1,089	1,655	1,855	2,135	2,288	2,502	2,893	56	16	6,733	10,610	58
Gross NPA (%)	7.97	7.38	6.97	5.96	5.21	3.97	2.66	-431bps	-131bps	5.97	1.95	-402bps
Net NPA (%)	3.69	2.99	2.55	2.28	1.91	1.36	0.89	-166bps	-47bps	2.28	0.63	-165bps
Deposits (Rs in bn)	644	654	669	687	712	736	762	14	3	687	790	15
Net Advances (Rs in bn)	500	514	532	553	576	602	617	16	3	553	641	16

Source: Company, Emkay Research

Exhibit 11: Revision in Estimates

Y/E Mar (Rs mn)	FY23E			FY24E			FY25E		
	Earlier	Revised	Change	Earlier	Revised	Change	Earlier	Revised	Change
Net income	41,164	43,277	5.1%	48,382	49,636	2.6%	56,853	58,167	2.3%
PPOP	20,828	23,029	10.6%	25,207	26,789	6.3%	30,198	32,136	6.4%
PAT	10,006	10,610	6.0%	13,038	13,240	1.5%	15,674	16,337	4.2%
EPS (Rs)	12.5	13.3	6.0%	16.3	16.5	1.5%	19.6	20.4	4.2%
BV (Rs)	105.5	106.2	0.7%	119.4	120.2	0.7%	136.3	137.6	0.9%

Source: Emkay Research

Exhibit 12: Key Assumptions

(%)	FY22A	FY23E	FY24E	FY25E
Loan Growth	9.9	15.9	17.2	19.2
Deposit Growth	8.5	15.0	16.7	18.9
NIM	3.7	4.1	4.0	3.9
GNPA	6.0	1.9	1.6	1.4
Credit Cost	1.3	1.2	1.1	1.1

Source: Emkay Research

Exhibit 13: Quarterly Summary

	3QFY21	4QFY21	1QFY22	2QFY22	3QFY22	4QFY22	1QFY23	2QFY23	3QFY23
Loans(Rs mn)	495,120	503,635	499,620	513,813	532,270	553,346	575,590	601,614	617,090
Growth YoY (%)	5.1	9.3	8.3	7.4	7.5	9.9	15.2	17.1	15.9
Growth QoQ (%)	3.5	1.7	(0.8)	2.8	3.6	4.0	4.0	4.5	2.6
Liability Profile & Margins									
Deposits (Rs mn)	620,900	632,784	643,980	654,101	668,710	686,762	711,680	736,141	761,750
Growth YoY (%)	(0.3)	7.1	7.2	7.0	7.7	8.5	10.5	12.5	13.9
Growth QoQ (%)	1.6	1.9	1.8	1.6	2.2	2.7	3.6	3.4	3.5
CASA (%)	34.6	34.2	35.0	35.4	36.1	34.8	36.4	35.2	33.9
CA (%)	10.9	10.2	10.0	10.7	11.1	10.1	11.2	10.9	10.3
SA (%)	23.8	24.0	25.0	24.8	25.0	24.7	25.2	24.3	23.5
Branches (no. of)	780	780	781	781	781	789	789	792	792
NIM (%)	3.29	3.46	3.55	3.74	3.68	3.79	3.82	4.07	4.32
Asset Quality (%)									
GNPA	7.4	7.9	8.0	7.4	7.0	6.0	5.2	4.0	2.7
NNPA	2.6	3.4	3.7	3.0	2.6	2.3	1.9	1.4	0.9
PCR	67.1	58.5	55.7	61.3	65.1	63.3	64.7	66.7	67.1
Capital Adequacy									
CRAR (%)	18.5	19.0	19.1	18.8	18.8	19.5	19.2	18.3	17.9
Tier I (%)	16.5	17.0	17.0	16.8	16.8	17.5	17.3	16.4	16.0
ROE Decomposition (%)									
NII	3.2	3.3	3.4	3.6	3.6	3.6	3.6	3.9	4.1
Other Income	1.1	1.2	1.1	0.9	1.0	1.0	1.0	1.1	1.4
Opex	3.2	3.1	2.3	2.5	2.5	2.4	2.3	2.3	2.4
PPOP	1.4	1.4	2.2	2.0	2.1	2.2	2.3	2.7	3.1
Provisioning Cost	1.1	0.4	1.3	0.9	0.8	0.7	0.8	1.1	1.7
PBT	0.3	1.0	0.9	1.1	1.3	1.5	1.6	1.6	1.5
ROA	0.2	0.6	0.6	0.9	1.0	1.1	1.1	1.2	1.3
ROE	2.0	6.0	6.2	9.3	10.2	11.4	11.9	12.7	14.3

Source: Company, Emkay Research

Key Financials (Standalone)

Income Statement

Y/E Mar (Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
Net interest income	**23,595**	**27,154**	**33,315**	**37,888**	**44,244**
Other income	**9,188**	**7,691**	**9,962**	**11,748**	**13,923**
Fee income	5,482	6,340	7,417	8,753	10,416
Net income	**32,783**	**34,844**	**43,277**	**49,636**	**58,167**
Operating expenses	19,868	18,542	20,248	22,847	26,031
Pre provision profit	**12,915**	**16,302**	**23,029**	**26,789**	**32,136**
PPP excl treasury	**10,746**	**16,804**	**23,781**	**26,413**	**31,572**
Provisions	7,571	6,993	9,427	9,096	10,304
Profit before tax	**5,344**	**9,309**	**13,602**	**17,693**	**21,832**
Tax	1,750	2,577	2,992	4,453	5,495
Tax rate	33	28	22	25	25
Profit after tax	**3,594**	**6,733**	**10,610**	**13,240**	**16,337**

Balance Sheet

Y/E Year End (Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
Equity	1,599	1,600	1,600	1,600	1,600
Reserves	67,999	74,362	83,372	94,532	108,469
Net worth	**69,598**	**75,962**	**84,972**	**96,132**	**110,069**
Deposits	632,784	686,762	789,621	921,358	1,095,067
Borrowings	20,413	8,521	10,651	13,314	16,642
Total liabilities	**746,233**	**800,437**	**917,933**	**1,068,683**	**1,266,775**
Cash and bank	31,241	35,943	39,015	47,751	59,259
Investments	160,189	172,161	192,521	217,852	252,489
Loans	503,635	553,346	641,197	751,717	896,010
Others	13,814	20,884	24,812	30,153	36,890
Total assets	**746,232**	**800,437**	**917,933**	**1,068,683**	**1,266,775**

Key Ratios (%)

Y/E Year End	FY21	FY22	FY23E	FY24E	FY25E
NIM	3.5	3.7	4.1	4.0	3.9
Non-II/avg assets	1.3	1.0	1.2	1.2	1.2
Fee income/avg assets	1.0	1.1	1.1	1.1	1.1
Opex/avg assets	2.8	2.4	2.4	2.3	2.2
Provisions/avg assets	1.1	0.9	1.1	0.9	0.9
PBT/avg assets	0.7	1.2	1.6	1.8	1.9
Tax/avg assets	0.2	0.3	0.3	0.4	0.5
RoA	0.5	0.9	1.2	1.3	1.4
RoAE	5.3	9.3	13.2	14.6	15.8
GNPA (%)	7.8	6.0	1.9	1.6	1.4
NNPA (%)	3.4	2.3	0.6	0.5	0.4

Per Share Data (Rs)	FY21	FY22	FY23E	FY24E	FY25E
EPS	4.5	8.4	13.3	16.5	20.4
BVPS	87.1	95.0	106.2	120.2	137.6
ABVPS	71.0	83.2	102.4	116.7	134.1
DPS	0.5	1.6	2.0	2.6	3.0

Valuations (x)	FY21	FY22	FY23E	FY24E	FY25E
PER	24.1	12.9	8.2	6.6	5.3
P/BV	1.5	1.3	1.1	0.9	0.8
P/ABV	1.5	1.3	1.1	0.9	0.8
P/PPOP	6.7	5.3	3.8	3.2	2.7
Dividend Yield (%)	0.5	1.5	1.8	2.4	2.8

Source: Company, Emkay Research

Growth (%)	FY21	FY22	FY23E	FY24E	FY25E
NII	0.5	15.1	22.7	13.7	16.8
PPOP	(26.7)	26.2	41.3	16.3	20.0
PAT	52.9	87.3	57.6	24.8	23.4
Loans	9.3	9.9	15.9	17.2	19.2

Quarterly (Rs mn)	Q3FY22	Q4FY22	Q1FY23	Q2FY23	Q3FY23
NII	6,872	7,099	7,459	8,214	8,890
NIM (%)	3.7	3.8	3.8	4.1	4.3
PPOP	4,016	4,413	4,755	5,723	6,890
PAT	1,855	2,135	2,288	2,502	2,893
EPS (Rs)	2.32	2.67	2.86	3.13	3.62

Source: Company, Emkay Research

Shareholding Pattern (%)	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22
Promoters	2.1	2.3	2.3	2.3	2.3
FIIs	18.9	15.5	15.4	15.4	16.5
DIIs	19.7	21.3	21.9	22.8	25.2
Public and Others	59.3	60.9	60.5	59.5	56.1

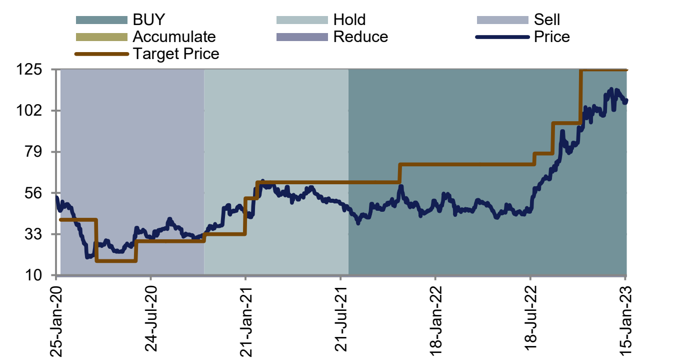
Source: Capitaline

RECOMMENDATION HISTORY (Rs/share)

Date	Closing Price	TP	Period	Rating	Analyst
22-Oct-22	91	125	12m	Buy	Anand Dama
3-Oct-22	79	95	12m	Buy	Anand Dama
30-Aug-22	69	95	12m	Buy	Anand Dama
26-Jul-22	59	78	12m	Buy	Anand Dama
22-May-22	45	72	12m	Buy	Anand Dama
1-Feb-22	51	72	12m	Buy	Anand Dama
11-Nov-21	58	72	12m	Buy	Anand Dama
5-Aug-21	47	62	12m	Buy	Anand Dama
1-Jun-21	56	62	12m	Hold	Anand Dama
12-Feb-21	55	62	12m	Hold	Anand Dama
20-Jan-21	46	53	12m	Hold	Anand Dama
3-Nov-20	32	33	12m	Hold	Anand Dama
1-Aug-20	35	29	12m	Sell	Anand Dama
26-Jun-20	37	29	12m	Sell	Anand Dama
11-Apr-20	28	18	12m	Sell	Anand Dama
3-Feb-20	47	41	12m	Sell	Anand Dama

Source: Company, Emkay Research

RECOMMENDATION HISTORY (Rs/share)



Source: Bloomberg, Company, Emkay Research

Emkay Rating Distribution

Ratings	Expected Return within the next 12-18 months.
BUY	Over 15%
HOLD	Between -5% to 15%
SELL	Below -5%

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Dissemination Date: 24 Jan 2023 01:13:37 (SGT)

Sources for all charts and tables are Emkay Research unless otherwise specified.

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