

HOLD Kotak Mahindra Bank

Your success is our success

Management transition to dwarf financial performance

BFSI - Banks ▶ Result Update ▶ October 23, 2023

TARGET PRICE (Rs): 1,955

Notwithstanding the sharp dip in NIMs (35bps QoQ) to 5.2%, KMB reported in-line PAT of Rs31.8bn/RoA of 2.5%. We believe the RBI's recent rebuke on unsecured loans (11% of loans) could slightly weigh on growth/margin. Further, KMB's Covid provision buffer stands low at 0.2% of loans vs 0.6-1.2% for peers and thus calls for higher provisions. We trim our estimates for FY25-26 a tad, and expect the bank to report moderate RoA/RoE of 2.1%/13%, respectively. The RBI has surprisingly given approval for the appointment of Ashok Vaswani (ex-Citi/Barclays), who has expertise in the Consumer, Corporate and Digital Banking space and has superseded KMB's internal candidates (EDs). As the bank's new MD & CEO, Mr Vaswani has the tall task of managing senior-management attrition/business dislocation (typically seen post top-management changes in banks) and filling the larger shoes of ex-CEO Uday Kotak. Factoring-in management transition-related risks, we cut TP multiple to 2.6x Sep-25E ABV from 2.8x Jun-25E ABV for the core bank and value the subsidiary at Rs480/share, leading to TP of Rs1,955/share (earlier Rs2,000) for KMB. We retain HOLD on the stock. The RBI not having yet objected to Uday Kotak's non-executive, non-independent board seat should provide some relief, though.

Kotak Mahindra Bank: Financial Snapshot (Standalone)

Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Net profit	85,727	1,09,393	1,29,450	1,40,759	1,53,132
Loan growth (%)	21.3	17.9	17.8	18.0	19.0
NII growth (%)	9.6	28.1	18.2	14.6	14.4
NIM (%)	4.3	4.9	5.0	4.9	4.7
PPOP growth (%)	2.5	23.2	26.2	15.1	14.3
Adj. EPS (Rs)	35.8	43.2	55.1	65.1	70.8
Adj. EPS growth (%)	14.9	20.9	27.5	18.3	8.7
Adj. BV (INR)	341.3	397.5	460.6	526.8	597.8
Adj. BVPS growth (%)	15.3	16.1	15.0	13.9	13.1
RoA (%)	2.1	2.4	2.4	2.3	2.1
RoE (%)	12.7	14.1	14.5	13.7	13.1
P/E (x)	29.8	23.4	19.8	18.2	16.7
P/ABV (x)	3.7	3.2	2.8	2.4	2.1

Source: Company, Emkay Research

Healthy growth, but margin sharply shrinks as CoF catches up

Credit growth was healthy at 18% YoY/6% QoQ, mainly led by strong traction in retail loans including unsecured loans, which contribute 11% of the loan portfolio (8.7% of loans). KMB expects growth to remain strong and is also determined to grow its unsecured book amid the rising risk on stress. Bank has recently acquired UP-based MFI *Sonata Finance* (as its business correspondent subsidiary), to bolster its MFI book (AUM: Rs19bn) and thus drive-in higher margin. Deposit growth too has been strong, at 23% YoY, but CASA slipped to 48% from the high range of the 50s and thus weighed on CoF. NIM contracted by 35bps QoQ to 5.2%, mainly due to the higher CoF. Going forward, margins could remain under pressure, in our view, as CoF continues to stay in catch-up mode, as do peers.

Slippages remain elevated, while contingent provision buffer negligible amid rising risk on unsecured loans

Slippages were higher than expected at Rs13bn/1.8% of loans for a second quarter in a row, due to grossing up of NPAs during the quarter, but better recovery/upgrades and credit growth led to slight improvement in GNPA ratio by 5bps QoQ to 1.7%. The restructured pool also declined, to Rs5.2bn/0.2% of loans (0.2% in 1Q)—the lowest among large peers. The bank continues to pull down its contingent buffer, which now stands at Rs3.2bn/0.1% of loans—one of the lowest among large banks. We believe the bank needs to shore-up the contingent buffer, given rising risk in unsecured loans and its otherwise unseasoned card/PL/CD portfolio. In addition to this, we expect the RBI to initiate action post the festive season, to curb undeterred growth in unsecured loans (mainly low-value), which would thus call for elevated provisioning.

The RBI clears Ashok Vaswani as the new MD & CEO, who has a big task on hands

In a surprising move, the RBI cleared the appointment of Ashok Vaswani as the MD & CEO of KMB, wef 1-Jan-2024 for three years, superseding the internal candidates (EDs). It is unclear if Mr Vaswani was the bank's preferred recommendation or his appointment is an unanticipated RBI decision. Notably, Mr Vaswani has a long & rich work experience in the Consumer, Corporate and Digital Banking arenas, given his long stint with global banks like Citigroup and Barclays as well as his recent leadership role in a US-Israeli AI firm. We believe the new MD & CEO has a tall task on his hands to manage senior management attrition/business dislocation, if any, typically seen post top-management changes in banks; meeting investors' high expectations as did the outgoing MD & CEO Uday Kotak is another cap to don for Mr Vaswani. However, there is some spot of relief for investors, as the RBI has not yet raised any objection to Uday Kotak's non-executive, non-independent board seat.

We retain HOLD

We expect KMB's RoA/RoE to normalize to 2.1%/13% from the highs of 2.4%/14.5% in FY23 due to margins/LLP normalization. Factoring-in management transition related risks, we lower our TP multiple to 2.6x Sep-25E ABV from 2.8x Jun-25E ABV for the core bank and value the subsidiary at Rs480/share, leading to TP at Rs1,955/share (earlier Rs2,000/share). Thus, we retain HOLD on the stock. **Downside risks:** Difficulty in mobilizing low-cost deposits, Management attrition and asset-quality risk in the unseasoned unsecured loan book.

Target Price – 12M	Sep-24
Change in TP (%)	(2.3)
Current Reco.	HOLD
Previous Reco.	HOLD
Upside/(Downside) (%)	10.5
CMP (20-Oct-23) (Rs)	1,769.6

Stock Data	Ticker
52-week High (Rs)	2,064
52-week Low (Rs)	1,644
Shares outstanding (mn)	1,987.5
Market-cap (Rs bn)	3,517
Market-cap (USD mn)	42,313
Net-debt, FY24E (Rs mn)	NA
ADTV-3M (mn shares)	4
ADTV-3M (Rs mn)	7,285.5
ADTV-3M (USD mn)	87.7
Free float (%)	74.0
Nifty-50	19,543
INR/USD	83.1
Shareholding, Jun-23	
Promoters (%)	25.9
FPIs/MFs (%)	39.9/21.3

Price Performance

(%)	1M	3M	12M
Absolute	(1.1)	(9.6)	(5.0)
Rel. to Nifty	0.7	(7.6)	(14.7)

1-Year share price trend (Rs)**Anand Dama**

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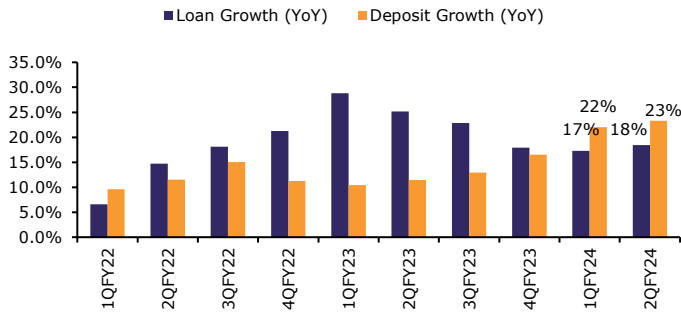
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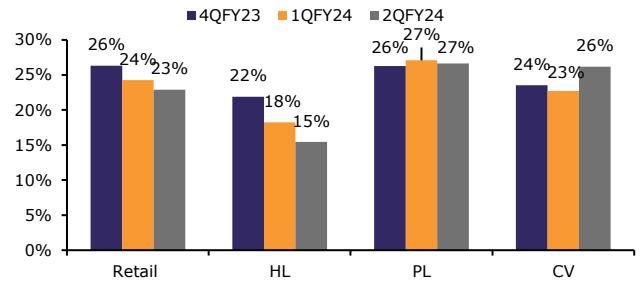
Story in Charts

Exhibit 1: Deposit and credit growth remains robust



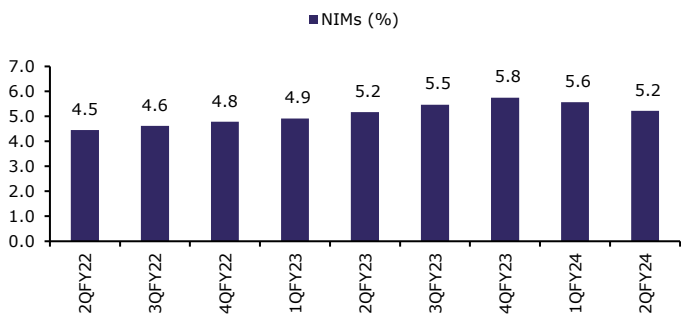
Source: Company, Emkay Research

Exhibit 2: Barring PL and CV, other segments within retail continue to witness moderation



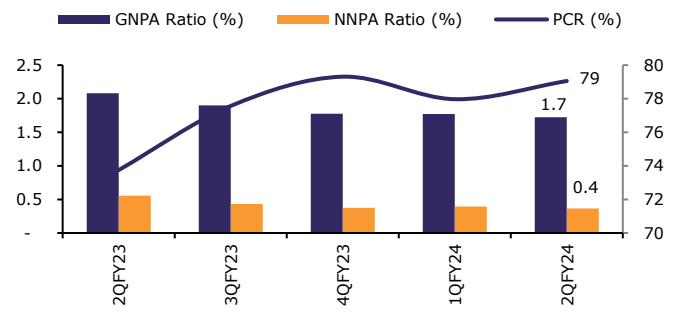
Source: Company, Emkay Research

Exhibit 3: Higher CoF led to contraction in NIMs



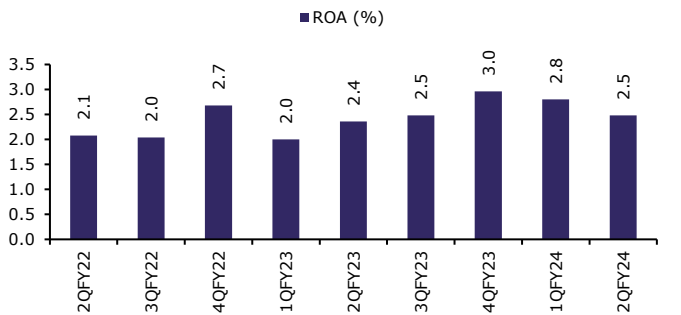
Source: Company, Emkay Research

Exhibit 4: Enhanced recovery/upgrades drove the slight improvement in GNPA ratio



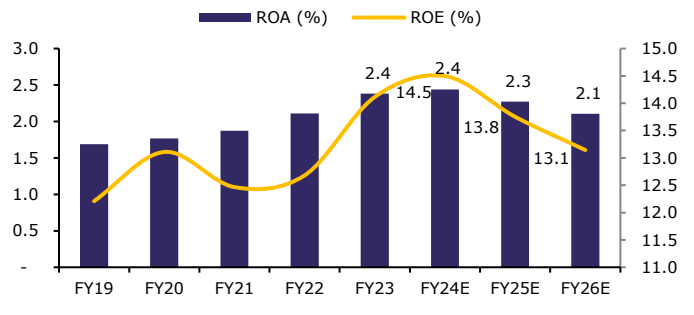
Source: Company, Emkay Research

Exhibit 5: Margin moderation and higher provisions caused a marginal decline in RoA



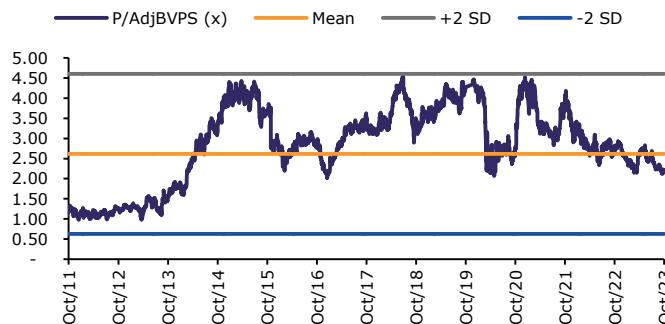
Source: Company, Emkay Research

Exhibit 6: We expect RoA/RoE to normalize due to moderation in margins/LLP



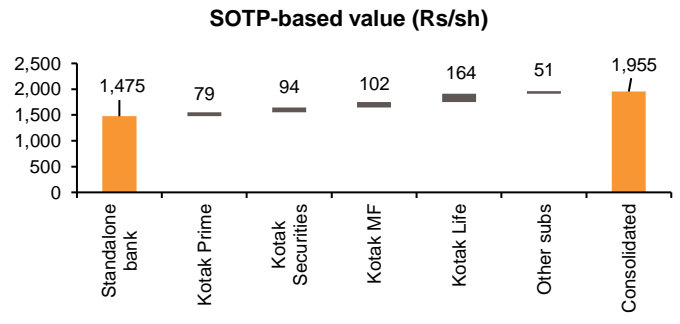
Source: Company, Emkay Research

Exhibit 7: The stock trades at 2.6x its one-year forward ABV



Source: Bloomberg, Emkay Research

Exhibit 8: SOTP-based valuation



Source: Emkay Research

Exhibit 9: Actuals vs Estimates (Q2FY24)

(Rs mn)	Actuals	Estimates		Variation		Comments
		Emkay	Consensus	Emkay	Consensus	
Net income	86,112	86,786	77,236	-1%	11%	Despite in-line NII, lower other income led to a shortfall
PPOP	46,101	45,857	44,678	1%	3%	Better optimization of opex led to a beat on PPOP
PAT	31,827	31,215	32,195	2%	-1%	Higher PPOP, partly offset by higher LLP led to an earnings beat

Source: Company, Emkay Research

Exhibit 10: Quarterly Summary

(Rs mn)	2QFY23	3QFY23	4QFY23	1QFY24	2QFY24	YoY (%)	QoQ (%)	FY23A	FY24E	YoY (%)
Interest Earned	80,928	89,986	98,209	1,05,000	1,11,928	38.3	6.6	3,42,509	4,55,841	33.1
Interest Exp	29,934	33,457	37,184	42,663	48,962	63.6	14.8	1,26,989	2,01,169	58.4
Net Interest Income	50,994	56,529	61,026	62,337	62,966	23.5	1.0	2,15,519	2,54,673	18.2
Global NIMs (reported)	5.17	5.47	5.75	5.57	5.22	5bps	-35bps	4.87	4.96	10bps
Non-interest Income	19,542	19,483	21,863	26,833	23,145	18.4	-13.7	70,830	1,01,368	43.1
Operating Expenses	34,861	37,514	36,415	39,674	40,011	14.8	0.8	1,37,870	1,68,595	22.3
Pre Provisioning Profit	35,675	38,498	46,474	49,496	46,101	29.2	-6.9	1,48,480	1,87,445	26.2
Provision & Contingencies	1,370	1,488	1,476	3,643	3,666	167.6	0.6	4,570	14,615	219.8
PBT	34,305	37,010	44,998	45,853	42,436	23.7	-7.5	1,43,910	1,72,830	20.1
Income Tax Expense (Gain)	8,498	9,091	10,042	11,330	10,526	23.9	-7.1	34,517	43,380	25.7
Net Profit/(Loss)	25,807	27,919	34,956	34,523	31,910	23.6	-7.6	1,09,393	1,29,450	18.3
Gross NPA (%)	2.08	1.90	1.78	1.77	1.72	-36bps	-5bps	1.78	1.58	-20bps
Net NPA (%)	0.55	0.43	0.37	0.40	0.37	-19bps	-3bps	0.37	0.38	1bps
Deposits (Rs bn)	3,252	3,447	3,631	3,863	4,010	23.3	3.8	3,631	4,314	18.8
Net Advances (Rs bn)	2,940	3,107	3,199	3,286	3,483	18.5	6.0	3,199	3,766	17.8

Source: Company, Emkay Research

Exhibit 11: Revision in Estimates

Y/E Mar (Rs mn)	FY24E			FY25E			FY26E		
	Earlier	Revised	Change	Earlier	Revised	Change	Earlier	Revised	Change
Net income	3,55,893	3,56,041	0.0%	4,08,516	4,12,760	1.0%	4,69,573	4,75,757	1.3%
PPOP	1,88,473	1,87,445	-0.5%	2,14,762	2,15,679	0.4%	2,45,875	2,46,482	0.2%
PAT	1,29,450	1,29,450	0.0%	1,42,834	1,40,759	-1.5%	1,55,360	1,53,132	-1.4%
EPS (Rs)	65.2	65.1	0.0%	71.9	70.8	-1.5%	78.2	77.0	-1.5%
BV (Rs)	481.1	480.8	0.0%	550.5	549.2	-0.2%	625.7	623.2	-0.4%

Source: Company, Emkay Research

Exhibit 12: Key Assumptions

(%)	FY23A	FY24E	FY25E	FY26E
Loan Growth	17.6	17.5	18.0	19.0
Deposit Growth	16.5	18.8	17.8	19.6
NIM	4.9	5.0	4.9	4.7
GNPA	1.8	1.6	1.6	1.7
Credit Cost	0.2	0.5	0.7	0.9
Yield on Advances	9.2	10.3	9.9	9.6
Cost of Deposits	3.5	4.7	4.4	4.2

Source: Emkay Research

Exhibit 13: Key Ratios and Trends

	2QFY22	3QFY22	4QFY22	1QFY23	2QFY23	3QFY23	4QFY23	1QFY24	2QFY24
Loans (Rs bn)	2,350	2,529	2,713	2,802	2,940	3,107	3,199	3,286	3,483
YoY growth (%)	14.7	18.1	21.3	28.8	25.1	22.9	17.9	17.3	18.5
QoQ growth (%)	8.0	7.6	7.2	3.3	4.9	5.7	2.9	2.7	6.0
Composition %									
- Corporate	27.8	26.9	25.6	25.4	22.3	23.3	22.6	23.6	23.5
- Retail & Agri	64.6	64.1	66.2	67.1	80.0	68.3	70.4	70.7	70.4
Liability Profile & Margins									
CASA %	60.6	59.9	60.7	58.1	56.2	53.3	52.8	49.0	48.3
CA %	18.3	18.7	20.7	18.0	18.5	18.5	19.3	16.8	17.2
SA %	42.3	41.2	39.9	40.1	37.7	34.8	33.5	32.3	31.1
NIM %	4.5	4.6	4.8	4.9	5.2	5.5	5.8	5.6	5.2
Branches	1,622	1,647	1,700	1,702	1,710	1,752	1,780	1,788	1850
Asset Quality (Rs mn)									
Gross NPA (Opening Balance)	79,318	76,579	69,828	64,697	63,786	62,102	59,946	57,683	59,092
GNPA	76,579	69,828	64,697	63,786	62,102	59,946	57,683	59,092	60,870
GNPA %	3.2	2.7	2.3	2.2	2.1	1.9	1.8	1.8	1.7
NPA	24,914	20,035	17,367	17,493	16,304	13,448	11,933	13,018	12,750
NNPA %	1.1	0.8	0.6	0.6	0.6	0.4	0.4	0.4	0.4
PCR %	66.8	70.8	72.6	72.3	73.3	77.2	79.0	77.7	78.8
Slippages (Rs mn)	12,930	7,500	7,360	14,350	9,830	7,480	8,230	12,050	13,140
Slippages % (annualized)	2.2%	1.2%	1.1%	2.0%	1.3%	1.0%	1.0%	1.5%	1.5%
Capital Adequacy (%)									
CAR	21.8	23.3	23.7	22.8	22.6	21.7	21.8	22.0	21.7
Tier I	20.8	22.4	21.7	21.6	21.5	20.7	20.6	20.9	20.6
ROE Decomposition (%)									
NII	4.0	4.2	4.3	4.4	4.7	5.0	5.1	5.0	4.8
Other Income (Ex Treasury)	1.8	1.8	1.8	2.0	1.8	1.5	1.6	1.9	1.8
Treasury	0.0	-0.5	-0.2	-0.8	0.0	0.3	0.2	0.2	0.0
Opex	2.7	2.9	2.7	3.0	3.2	3.3	3.1	3.2	3.1
PPOP	3.1	2.6	3.2	2.6	3.3	3.4	3.9	3.9	3.5
Provisioning Cost	0.4	-0.1	-0.3	0.0	0.1	0.1	0.1	0.3	0.3
PBT	2.7	2.7	3.4	2.6	3.2	3.3	3.8	3.7	3.2
ROA	2.0	2.1	2.6	1.9	2.4	2.5	2.9	2.8	2.4
ROE	12.1	12.2	15.3	11.1	13.4	14.0	16.7	15.9	14.2

Source: Company, Emkay Research

Kotak Mahindra Bank: Standalone Financials and Valuations

Profit & Loss					
Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Interest Income	2,70,388	3,42,509	4,55,841	5,13,905	5,80,185
Interest Expense	1,02,209	1,26,989	2,01,169	2,21,940	2,46,319
Net interest income	1,68,179	2,15,519	2,54,673	2,91,966	3,33,866
NII growth (%)	9.6	28.1	18.2	14.6	14.4
Other income	59,859	70,830	1,01,368	1,20,795	1,41,891
Total Income	2,28,038	2,86,350	3,56,041	4,12,760	4,75,757
Operating expenses	1,07,530	1,37,870	1,68,595	1,97,081	2,29,274
PPOP	1,20,509	1,48,480	1,87,445	2,15,679	2,46,482
PPOP growth (%)	2.5	23.2	26.2	15.1	14.3
Core PPOP	1,14,896	1,20,518	1,56,037	1,81,400	2,07,820
Provisions & contingencies	6,896	4,570	14,615	27,750	42,033
PBT	1,13,613	1,43,910	1,72,830	1,87,929	2,04,449
Extraordinary items	0	0	0	0	0
Tax expense	27,886	34,517	43,380	47,170	51,317
Minority interest	0	0	0	0	0
Income from JV/Associates	0	0	0	0	0
Reported PAT	85,727	1,09,393	1,29,450	1,40,759	1,53,132
PAT growth (%)	23.1	27.6	18.3	8.7	8.8
Adjusted PAT	85,727	1,09,393	1,29,450	1,40,759	1,53,132
Diluted EPS (Rs)	43.0	55.1	65.1	70.8	77.0
Diluted EPS growth (%)	22.4	28.0	18.3	8.7	8.8
DPS (Rs)	1.1	1.5	2.0	2.5	3.0
Dividend payout (%)	2.6	2.5	2.7	3.1	3.5
Effective tax rate (%)	24.5	24.0	25.1	25.1	25.1
Net interest margins (%)	4.3	4.9	5.0	4.9	4.7
Cost-income ratio (%)	47.2	48.1	47.4	47.7	48.2
Shares outstanding (mn)	1,984.7	1,986.6	1,987.5	1,987.5	1,987.5

Source: Company, Emkay Research

Asset quality and other metrics					
Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Asset quality					
Gross NPLs	64,697.4	57,683.2	60,161.1	74,015.9	93,420.4
Net NPLs	17,367.1	11,933.0	14,438.7	19,984.3	28,026.1
GNPA ratio (%)	2.3	1.8	1.6	1.6	1.7
NNPA ratio (%)	0.6	0.4	0.4	0.4	0.5
Provision coverage (%)	73.2	79.3	76.0	73.0	70.0
Gross slippages	17,971.3	18,582.1	19,952.4	33,949.7	54,883.0
Gross slippage ratio (%)	1.3	1.1	1.0	1.5	2.4
LLP ratio (%)	0.3	0.2	0.5	0.7	0.9
NNPA to networth (%)	2.4	1.4	1.5	1.8	2.2
Capital adequacy					
Total CAR (%)	23.7	21.8	21.0	20.6	19.9
Tier-1 (%)	21.7	20.6	20.0	19.7	19.2
CET-1 (%)	21.5	19.0	18.7	18.6	18.2
RWA-to-Total Assets (%)	77.7	76.0	78.0	78.0	78.0
Miscellaneous					
Total income growth (%)	3.7	25.2	34.8	13.9	13.8
Opex growth (%)	25.3	28.2	22.3	16.9	16.3
Core PPOP growth (%)	4.9	29.5	16.3	14.6	14.4
PPOP margin (%)	36.5	35.9	33.6	34.0	34.1
PAT/PPOP (%)	71.1	73.7	69.1	65.3	62.1
LLP-to-Core PPOP (%)	6.0	3.8	9.4	15.3	20.2
Yield on advances (%)	7.9	9.2	10.3	9.9	9.6
Cost of funds (%)	3.2	3.5	4.8	4.4	4.2

Source: Company, Emkay Research

Balance Sheet					
Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Share capital	9,923	9,933	9,938	9,938	9,938
Reserves & surplus	7,09,955	8,20,270	9,50,743	10,86,497	12,33,604
Net worth	7,19,878	8,30,203	9,60,681	10,96,435	12,43,541
Deposits	31,16,841	36,30,961	43,13,637	50,79,973	60,78,085
Borrowings	2,59,671	2,34,163	2,74,124	3,16,093	3,64,206
Interest bearing liab.	33,76,512	38,65,123	45,87,761	53,96,066	64,42,291
Other liabilities & prov.	1,97,894	2,03,299	1,66,964	1,92,777	1,78,327
Total liabilities & equity	42,94,284	48,98,625	57,15,406	66,85,277	78,64,159
Net advances	27,12,536	31,98,612	37,66,403	44,44,277	52,87,593
Investments	10,05,802	12,14,037	14,07,797	16,35,256	18,89,245
Cash, other balances	4,29,239	3,25,423	3,76,739	4,31,685	5,02,499
Interest earning assets	36,83,959	41,47,578	47,38,072	55,50,939	65,11,218
Fixed assets	16,437	19,203	19,700	22,274	25,216
Other assets	1,30,269	1,41,349	1,44,767	1,51,784	1,59,608
Total assets	42,94,284	48,98,625	57,15,406	66,85,277	78,64,159
BVPS (Rs)	363.0	418.1	481.0	549.2	623.2
Adj. BVPS (INR)	341.3	397.5	460.6	526.8	597.8
Gross advances	27,59,866	32,44,362	38,12,126	44,98,308	53,52,987
Credit to deposit (%)	87.0	88.1	87.3	87.5	87.0
CASA ratio (%)	60.7	52.8	47.6	45.3	45.1
Cost of deposits (%)	3.1	3.5	4.7	4.4	4.2
Loans-to-Assets (%)	63.2	65.3	65.9	66.5	67.2
Net advances growth (%)	21.3	17.9	17.8	18.0	19.0
Deposit growth (%)	11.3	16.5	18.8	17.8	19.6
Book value growth (%)	11.8	15.2	15.0	14.2	13.5

Source: Company, Emkay Research

Valuations and key Ratios					
Y/E Mar	FY22	FY23	FY24E	FY25E	FY26E
P/E (x)	29.8	23.4	19.8	18.2	16.7
P/B (x)	3.7	3.2	2.8	2.4	2.1
P/ABV (x)	3.8	3.2	2.8	2.4	2.2
P/PPOP (x)	29.2	23.7	18.8	16.3	14.3
Dividend yield (%)	0.1	0.1	0.1	0.1	0.2
DuPont-RoE split (%)					
NII/avg assets	4.1	4.7	4.8	4.7	4.6
Other income	1.5	1.5	1.9	1.9	2.0
Fee income	1.0	1.2	1.3	1.4	1.4
Opex	2.6	3.0	3.2	3.2	3.2
PPOP	3.0	3.2	3.5	3.5	3.4
Core PPOP	3.1	3.0	3.4	3.4	3.4
Provisions	0.2	0.1	0.3	0.4	0.6
Tax expense	0.7	0.8	0.8	0.8	0.7
RoA (%)	2.1	2.4	2.4	2.3	2.1
Leverage ratio (x)	6.0	5.9	5.9	6.1	6.2
RoE (%)	12.7	14.1	14.5	13.7	13.1
Quarterly data					
Rs mn, Y/E Mar	Q2FY23	Q3FY23	Q4FY23	Q1FY24	Q2FY24
NII	50,994	56,529	61,026	62,337	62,966
NIM (%)	5.2	5.5	5.8	5.6	5.2
PPOP	35,675	38,498	46,474	49,496	46,101
PAT	25,807	27,919	34,956	34,523	31,827
EPS (Rs)	13.00	14.06	17.60	17.38	16.02

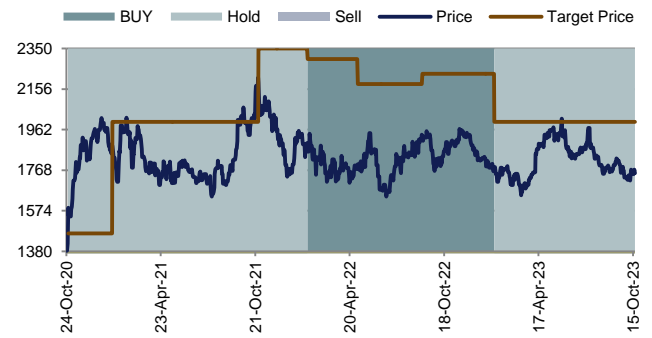
Source: Company, Emkay Research

RECOMMENDATION HISTORY - DETAILS

Date	CMP (INR)	TP (INR)	Rating	Analyst
23-Jul-23	1,970	2,000	Hold	Anand Dama
30-Apr-23	1,938	2,000	Hold	Anand Dama
09-Mar-23	1,717	2,000	Hold	Anand Dama
22-Jan-23	1,763	2,000	Hold	Anand Dama
24-Oct-22	1,896	2,230	Buy	Anand Dama
06-Sep-22	1,916	2,230	Buy	Anand Dama
23-Jul-22	1,827	2,180	Buy	Anand Dama
26-May-22	1,909	2,180	Buy	Anand Dama
05-May-22	1,798	2,180	Buy	Anand Dama
29-Jan-22	1,898	2,300	Buy	Anand Dama
27-Oct-21	2,188	2,350	Hold	Anand Dama
27-Jul-21	1,698	2,000	Hold	Anand Dama
03-May-21	1,725	2,000	Hold	Anand Dama
25-Jan-21	1,794	2,000	Hold	Anand Dama
20-Jan-21	1,884	2,000	Hold	Anand Dama
27-Oct-20	1,588	1,465	Hold	Anand Dama

Source: Company, Emkay Research

RECOMMENDATION HISTORY - TREND



Source: Company, Bloomberg, Emkay Research

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