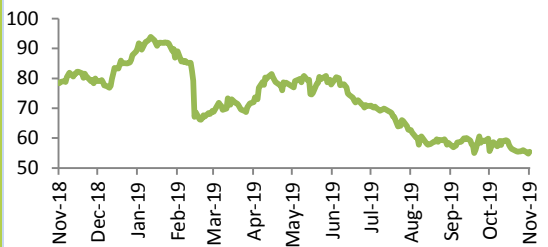


**Karur Vysya Bank Ltd.**

Recommendation	HOLD
CMP	Rs. 58
Target Price	Rs. 80
Sector	Banking

Stock Details	
BSE Code	590003
NSE Code	KARURVYSYA
Bloomberg Code	KVB IN
Market Cap (Rs Cr)	Rs. 4,622
Free Float (%)	97.9%
52- week H/L (Rs)	95/51
Avg. volume (BSE+NSE)	1044270
Face Value (Rs)	2
Div per share (FY 19)	0.60
Shares o/s (Cr)	79.9

Relative Performance (%)	1Mth	3Mth	1Yr
<b>KVB</b>	-0.4%	-11.6%	-29.3%
<b>Sensex</b>	4.9%	8.5%	16.7%



Shareholding Pattern		Sep'19
Promoters Holding		2.1%
Institutional (Incl. FII)		42.8%
Public & others		55.1%

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Year	NII (Rs cr)	Growth (%)	PBP (Rs cr)	PAT (Rs cr)	Growth (%)	EPS (Rs)	PE (x)	Adj BVPS (Rs)	P/ABV (x)	RoE (%)
FY18	2,298	11%	1,777	346	-43%	4.8	13.8	60.6	1.1	6.1%
FY19	2,363	3%	1,711	211	-39%	2.6	24.9	50.1	1.3	3.3%
FY20E	2,473	5%	1,769	288	37%	3.6	18.2	59.0	1.1	4.4%
FY21E	2,832	15%	2,025	676	135%	8.5	7.8	66.5	1.0	9.7%

**Growth takes a back seat with rundown of higher ticket SME/Corp segments**

- Advances continued to grow at a sluggish rate of 3% YoY and stood at Rs. 49,388 Cr vs. Rs. 48,141 Cr in Q2FY19. Retail loans continued to exhibit robust growth momentum at 33% YoY contributing 24% to the overall advances vs 18% YoY. The bank continued to maintain a cautious stance on Agri (-1% YoY), SME (-3% YoY) and Corporate (-8% YoY) with each contributing 17%, 33% and 27% resp. We expect loan growth of 9% CAGR over FY19-21E.
- NIMs were down 11 bps YoY and stood at 3.46% (lowest in the last 14 qtrs.) despite improvement in yields on advances by 6bps YoY, as the bank held excess liquidity of ~Rs. 6000 Cr.
- Fee income took a hit as the bank is intentionally slowing down the large ticket loans which generate higher fee income. Total income grew by 16% YoY on the back of profit made on sale of investments; non-interest income grew by 58% YoY.
- Opex growth stood at 13% YoY. Cost/income ratio at 50.7% declined by 140bps YoY, but continued to be elevated on QoQ basis (+280bps).
- PBP increased by 19% YoY to Rs. 431.2 Cr.
- Provisions came at Rs. 365 Cr vs expectation of Rs. 335 Cr, YoY Rs. 213 Cr and QoQ Rs. 330 Cr. Credit cost for the quarter stood at 3.0% vs 2.7% QoQ & 1.8% YoY. Credit costs are expected to remain elevated in FY20E as the bank targets to increase PCR from current level of 49% to 55-60%.
- The bank reported Net Profit of Rs. 63 Cr vs. Rs. 83 Cr in Q2FY19 (-24% YoY) and Rs. 73 Cr in Q4FY19 (-13% QoQ).

**Valuation and Outlook**

Sharpening focus on the Retail segment and taking a cautious stance by slowing down advances to the Corporate and SME segment while building revenue as well as profit momentum (loan/PAT CAGR of 9%/79%, respectively, over FY19-21E) and transformation into a granular and higher RoE business combined with cheap valuations at 1.2x FY21E ABV provides decent scope for re-rating in the long term. However, continued elevated stress in the Corporate and SME books combined with higher credit costs in order to shore up the PCR, should translate to sub optimal ROA in FY20E. **We maintain our 'HOLD' rating on the stock with a price target of Rs. 80, based on 1.3x FY21E ABV (20% discount to DCB).**

## Karur Vysya Bank Ltd.

### Quarterly Results

Particulars (Rs. Cr)	Q2FY18	Q3FY18	Q4FY18	Q1FY19	Q2FY19	Q3FY19	Q4FY19	Q1FY20	Q2FY20	Comments
Interest Earned	1402	1422	1491	1443	1457	1443	1474	1493	1538	<i>NIMs were down 11 bps YoY and stood at 3.46% (lowest in the last 14 qtrs.) despite improvement in yields on advances by 6bps YoY, as the bank held excess liquidity</i>
Interest Expended	847	861	848	859	878	862	854	909	941	
Net Interest Income	555	562	643	584	579	581	619	584	596	
<i>Growth</i>	12%	9%	11%	8%	4%	3%	-4%	0%	3%	
NIMs	3.81%	3.76%	4.13%	3.65%	3.57%	3.60%	3.88%	3.49%	3.46%	
Other Income	230	225	209	255	176	260	272	270	278	
% of total income	29%	29%	25%	30%	23%	31%	31%	32%	32%	
Total Income	785	786	852	838	755	841	892	854	874	
<i>Growth</i>	10%	14%	5%	8%	-4%	7%	5%	2%	16%	
Employee exp	155	153	179	179	173	198	212	204	213	
Other op exp	203	212	193	200	221	218	215	205	230	
<b>Total op exp</b>	<b>358</b>	<b>365</b>	<b>372</b>	<b>379</b>	<b>393</b>	<b>416</b>	<b>427</b>	<b>409</b>	<b>443</b>	
<i>Growth</i>	-9%	-12%	22%	16%	10%	14%	15%	8%	13%	
<b>Cost to income ratio</b>	<b>45.6%</b>	<b>46.4%</b>	<b>43.7%</b>	<b>45.2%</b>	<b>52.1%</b>	<b>49.4%</b>	<b>47.9%</b>	<b>47.9%</b>	<b>50.7%</b>	<i>Provisions came at Rs. 365 Cr vs expectation of Rs. 335 Cr, YoY Rs. 213 Cr and QoQ Rs. 330 Cr. Credit cost for the quarter stood at 3.0% vs 2.7% QoQ &amp; 1.8% YoY.</i>
Profit before prov.	427	421	480	460	361	425	465	445	431	
Provisions	321	325	394	423	213	400	352	330	365	
<i>Growth</i>	170%	244%	81%	81%	-34%	23%	-11%	-22%	71%	
Credit Cost	3.07%	3.12%	3.61%	3.75%	1.85%	3.46%	2.92%	2.72%	3.00%	
Profit before tax	106	96	86	37	148	25	112	115	66	
Tax	30	25	35	-9	65	3	52	42	3	
<b>Profit after tax</b>	<b>75.6</b>	<b>71.5</b>	<b>50.6</b>	<b>45.9</b>	<b>83.7</b>	<b>21.2</b>	<b>60.0</b>	<b>72.9</b>	<b>63.3</b>	
<i>Growth</i>	-40%	-38%	-77%	-69%	11%	-70%	19%	59%	-24%	
No. of shares	60.9	72.7	72.7	72.7	79.9	79.9	79.9	79.9	79.9	
EPS	1.2	1.0	0.7	0.6	1.0	0.3	0.8	0.9	0.8	
Advances	44,237	44,836	45,973	47,886	48,140	47,766	50,616	49,182	49,388	
<i>Growth</i>	12%	17%	11%	13%	9%	7%	10%	3%	3%	
CASA Ratio	27.6%	28.1%	29.1%	30.0%	29.5%	29.8%	29.9%	29.7%	28.7%	
CAR	12.2%	13.9%	14.4%	14.1%	0.1%	0.1%	0.2%	16.0%	16.0%	
Slippages	427	713	629	785	190	888	480	474	417	
<i>Slippage Ratio</i>	3.9%	6.4%	5.5%	6.6%	1.6%	7.4%	3.8%	3.9%	3.4%	
Gross NPA	4.8%	5.9%	6.6%	7.4%	7.7%	8.5%	8.8%	9.2%	8.9%	
Net NPA	3.2%	3.9%	4.2%	4.4%	4.4%	5.0%	5.0%	4.9%	4.5%	
PCR (Calculated)	34.1%	36.2%	38.2%	41.4%	44.7%	43.4%	45.6%	48.5%	51.8%	
<b>ROA</b>	<b>0.5%</b>	<b>0.4%</b>	<b>0.3%</b>	<b>0.3%</b>	<b>0.5%</b>	<b>0.3%</b>	<b>0.3%</b>	<b>0.4%</b>	<b>0.3%</b>	
<b>ROE</b>	<b>5.8%</b>	<b>4.6%</b>	<b>3.2%</b>	<b>2.9%</b>	<b>5.3%</b>	<b>1.3%</b>	<b>3.7%</b>	<b>4.5%</b>	<b>3.9%</b>	

Source: Company, NBRR

## Key Conference-call highlights and our takeaways

### ✦ Asset Quality continues to remain under stress

- a) GNPA came at Rs. 4391 Cr vs QoQ Rs. 4510.8 Cr at 8.89% vs QoQ 9.17%. GNPA reduced QoQ as recoveries exceeded gross slippages.
- b) Gross Slippages came at Rs. 417 Cr (3.4%) vs Rs. 474 Cr QoQ (3.9%) while recoveries were at Rs. 536 Cr (4.3%) vs Rs. 413 Cr (3.4%) QoQ. Higher recoveries are partly due to sale to ARC worth Rs. 192 Cr. Thus net slippages were Rs. -119 Cr, significantly below the management's earlier guidance of ~Rs. 220 Cr each quarter in Q4FY19.
- c) The management has also indicated that the Gross slippages would be higher at ~Rs. 2200 Cr (vs previous guidance of Rs. 1850 Cr given in Q3FY19). Stress in one of the large corporates where the bank has a large exposure and a restructured account will result in higher slippages. The combined exposure to these entities is Rs.230 Cr.
- d) SME & Corporate slippages remained elevated at 4.5%/7.2%. Slippage in corporate segment is from a large NBFC. NBFC/RE exposure is 4%/6% of the total book. **We believe the management will be able to contain net slippages at well below Rs. 1100 Cr for the 5 quarter period from Q4FY19 to Q4FY20 (as per the management's previous guidance).**
- e) The bank has stopped disbursement to the owners of Warehouses where it has been seeing stress in the past few quarters. The management expects no further losses in this segment where the exposure of the bank stands at Rs. 200 Cr.
- f) Provisions came at Rs. 365 Cr vs expectation of Rs. 335 Cr, YoY Rs. 213 Cr, QoQ Rs. 330 Cr. Credit cost for the quarter stood at 3.0% vs 2.7% QoQ & 1.8% YoY.
- g) Calculated PCR improved to 50.6% vs 47.0% QoQ and 42.9% YoY. Management has maintained that it will aggressively provision till it achieves a calculated PCR of 55-60%.

## Karur Vysya Bank Ltd.

### Operational Highlights

- a) Advances stood at Rs. 49,388 Cr vs Rs. 48,140 Cr YoY, a tepid growth of 3% YoY. Retail loans continued to maintain its growth momentum at 33% YoY (ex-IBPC growth was 28%) contributing 24% to the overall advances vs. 18% YoY. The bank chose to grow cautiously in Agri (-1% YoY), SME (-3% YoY) and Corporate (-8% YoY) with each contributing 17%, 33% and 27% respectively.
- b) Retail loans would continue the positive upward trajectory. On the commercial side, substantial growth is expected from small ticket loans. **Loan growth guidance has again been lowered from low teens to 10% for FY20 (in previous quarter, it was lowered from mid-teens to low teens).**
- c) Deposit growth was considerable and the bank raised time deposits (retail) with a view to stay liquid in times of tight liquidity. Total deposits grew 7% YoY. CASA ratio declined 100 bps QoQ & 80 bps YoY to 28.7%.
- d) Treasury assets have increased to ~Rs. 21,000cr from ~Rs. 15,000 Cr as on FY19. This has pulled down the NIMs by 11 bps YoY and 3 bps QoQ to 3.46%.
- e) Fee income has seen slowdown on the asset customers. The large ticket assets which were larger fee payers have come down. Challenge on the no funded business especially in the Infra space, which is being brought down intentionally reducing the fee income
- f) Majority of Agri loans are essentially gold loans.
- g) 90% of loans were approved digitally in Retail & Commercial segments during the quarter. The management expects the applications for retail loans through the digital platform to double in H2FY20.

## Karur Vysya Bank Ltd.

### Valuation & View

- Despite KVBs stellar performance in its core segment of Retail & SME historically, its decision to aggressively grow the corporate book over FY07-12 and the subsequent stress due to defaults landed the bank in trouble. Since FY14, KVB has shifted its focus back towards Retail & SME. The bank has now further reduced its dependence on more risky larger ticket size loans and intentionally shifting to smaller ticket size loans.
- The credit cost is expected to remain elevated in FY20E at 2.4%. Although our long term thesis remains intact for KVB, any meaningful improvement in the bank's return ratios can only be expected from FY21E onwards.
- FY20E would see an improvement in return ratios with the bank would report higher profits on the back of adoption of lower tax rate of ~25% vs the previous tax rate of ~34%.
- As compared to its peers DCB Bank and City Union Bank (CUB), KVB trades at a discount due to below par asset quality, muted loan growth, elevated credit costs and poor return ratios. DCB trades at 1.5x FY21E P/BV with a RoA of 1.1% and RoE of 13.7%. CUB trades at 2.5x FY21E P/BV with RoA of 1.6% and RoE of 15.3%.
- Sharpening focus on the Retail segment and by slowing down advances to the Corporate and SME segment while building revenue as well as profit momentum (loan/PAT CAGR of 9%/79%, respectively, over FY19-21E) and transformation into a granular and higher RoE business combined with cheap valuations at 0.9x FY21E ABV provides decent scope for re-rating in the long term. However, continued elevated stress in the Corporate and SME books combined with higher credit costs in order to shore up the PCR, should translate to sub optimal ROA in FY20E. **We maintain our 'HOLD' rating on the stock with a price target of Rs. 80, based on 1.2x FY21E ABV (20% discount to DCB).**

### Dupont ROE

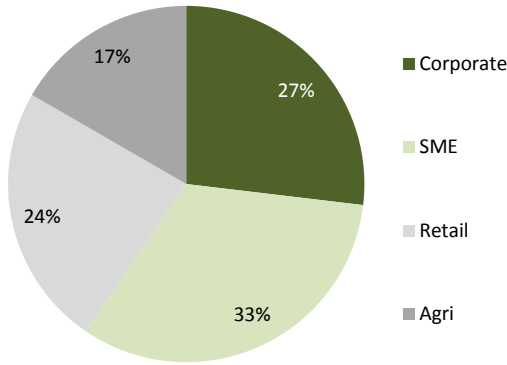
	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
NII	2.75%	2.61%	2.80%	3.18%	3.43%	3.57%	3.47%	3.30%	3.40%
Other Income	1.07%	1.15%	1.11%	1.26%	1.30%	1.40%	1.41%	1.42%	1.37%
Total Income	3.8%	3.8%	3.9%	4.4%	4.7%	5.0%	4.9%	4.7%	4.8%
Opex	1.81%	2.06%	2.11%	2.11%	2.13%	2.21%	2.37%	2.36%	2.34%
PPP	2.0%	1.7%	1.80%	2.3%	2.6%	2.8%	2.5%	2.4%	2.4%
Provisions	0.29%	0.90%	0.92%	0.70%	1.14%	1.98%	2.04%	1.85%	1.35%
PBT	1.7%	0.8%	0.9%	1.6%	1.5%	0.8%	0.5%	0.5%	1.1%
Tax Rate	0.4%	0.0%	0.0%	0.61%	0.46%	0.24%	0.2%	0.1%	0.3%
ROA	1.30%	0.79%	0.85%	1.01%	1.00%	0.54%	0.31%	0.39%	0.81%
Leverage	12.8	15.3	13.8	12.7	12.6	11.4	10.7	11.4	12.0
ROE	16.7%	12.1%	11.8%	12.9%	12.6%	6.1%	3.3%	4.4%	9.7%

Source: Company, NBRR

## Karur Vysya Bank Ltd.

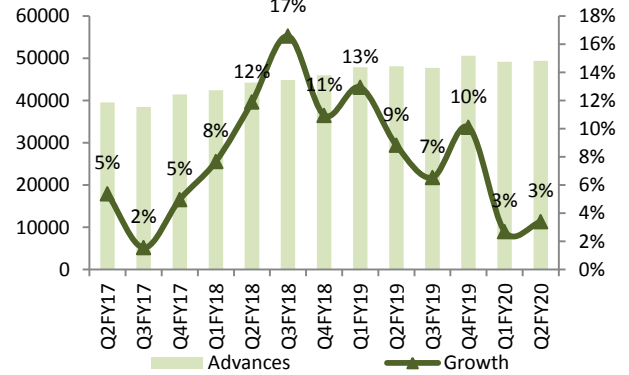
### Story in Charts

**Portfolio mix leaning towards granular loans**



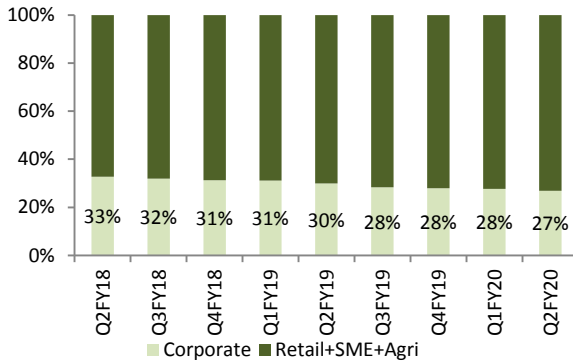
Source: Company, NBRR

**Muted Advances growth**



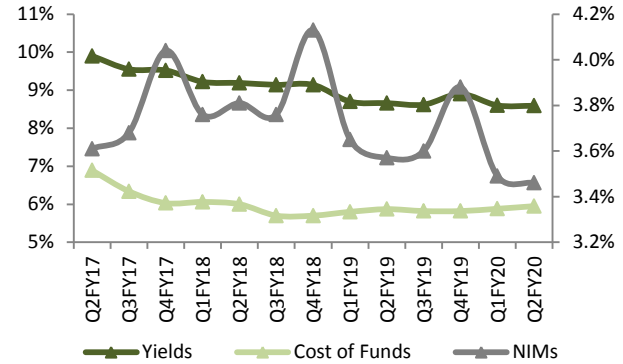
Source: Company, NBRR

**Declining share of corporate advances**



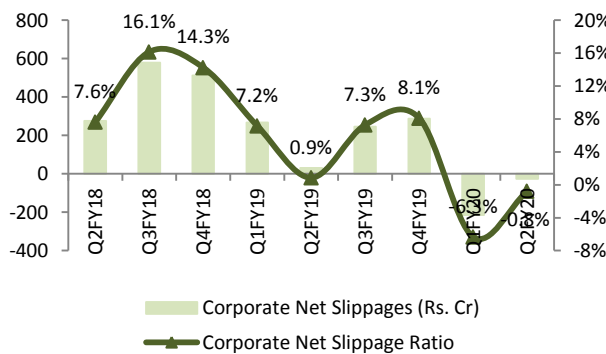
Source: Company, NBRR

**NIMS were affected by excess liquidity**



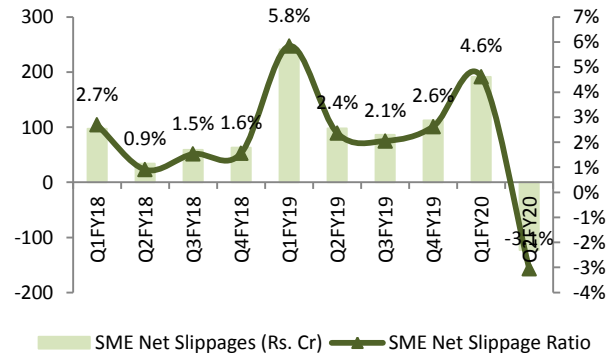
Source: Company, NBRR

**Corporate Net Slippages lower due to recoveries**



Source: Company, NBRR

**SME Net Slippages declined due to recoveries**



Source: Company, NBRR

## Karur Vysya Bank Ltd.

## Financials

P&L (Rs. Crs)	FY17	FY18	FY19	FY20E	FY21E
Interest earned	5,622	5,700	5,816	6,430	7,247
Interest expended	3,549	3,402	3,453	3,957	4,414
<b>NII</b>	<b>2,074</b>	<b>2,298</b>	<b>2,363</b>	<b>2,473</b>	<b>2,832</b>
Non interest income	782	900	963	1,065	1,141
<b>Total income</b>	<b>2,856</b>	<b>3,198</b>	<b>3,326</b>	<b>3,538</b>	<b>3,974</b>
<b>Growth</b>	<b>15%</b>	<b>12%</b>	<b>4%</b>	<b>6%</b>	<b>12%</b>
Operating expenses	1,285	1,421	1,615	1,768	1,948
<i>Growth</i>	<i>8%</i>	<i>11%</i>	<i>14%</i>	<i>10%</i>	<i>10%</i>
<i>Staff costs</i>	<i>608</i>	<i>639</i>	<i>761</i>	<i>878</i>	<i>967</i>
<i>Other Op Exp</i>	<i>677</i>	<i>782</i>	<i>854</i>	<i>891</i>	<i>981</i>
<b>Profit before prov</b>	<b>1,571</b>	<b>1,777</b>	<b>1,711</b>	<b>1,769</b>	<b>2,025</b>
<b>Growth</b>	<b>21%</b>	<b>13%</b>	<b>-4%</b>	<b>3%</b>	<b>14%</b>
Provisions	687	1,274	1,389	1,384	1,122
<i>Growth</i>	<i>85%</i>	<i>85%</i>	<i>9%</i>	<i>0%</i>	<i>-19%</i>
Profit before tax	884	504	322	385	904
Taxes	278	158	111	97	227
<b>Net profit</b>	<b>606</b>	<b>346</b>	<b>211</b>	<b>288</b>	<b>676</b>
<b>Growth</b>	<b>7%</b>	<b>-43%</b>	<b>-39%</b>	<b>37%</b>	<b>135%</b>

Key Ratios	FY17	FY18	FY19	FY20E	FY21E
Yield on Advances	11.3%	10.3%	9.8%	9.8%	10.0%
Yield on Tot Assets	9.6%	9.1%	8.7%	8.8%	8.9%
Cost of Borrowings	6.5%	5.9%	5.7%	5.9%	5.9%
Spread	4.82%	4.39%	4.05%	3.94%	4.10%
NIM	3.70%	3.87%	3.68%	3.50%	3.60%

Profitability Ratios	FY17	FY18	FY19	FY20E	FY21E
Cost / Income Ratio	45.0%	44.4%	48.6%	50.0%	49.0%
ROE	12.0%	6.1%	3.3%	4.4%	9.7%
ROA	1.00%	0.54%	0.31%	0.39%	0.81%

Per Share Data	FY17	FY18	FY19	FY20E	FY21E
EPS	9.9	4.8	2.6	3.6	8.5
BVPS	82.6	86.2	80.4	83.2	90.5
Adjusted BVPS	65.7	60.6	50.1	59.0	66.5

Bal. Sheet (Rs. Crs)	FY17	FY18	FY19	FY20E	FY21E
Equity capital	122	145	160	160	160
Reserves & surplus	4,914	6,119	6,263	6,494	7,074
Net worth	5,036	6,264	6,423	6,654	7,234
Deposits	53,700	56,890	59,868	68,872	73,917
<i>(of which CASA)</i>	<i>14,889</i>	<i>16,577</i>	<i>17,915</i>	<i>19,423</i>	<i>21,200</i>
Borrowings	1,696	2,382	1,565	3,065	3,315
Other liab and prov	1,376	1,393	1,484	1,734	1,759
Total liabilities	56,772	60,665	62,917	73,671	78,991
<b>Total liab and equity</b>	<b>61,808</b>	<b>66,929</b>	<b>69,340</b>	<b>80,324</b>	<b>86,225</b>
Cash and bank bal	1,555	1,337	762	2,412	2,262
Bal. with RBI	2,790	2,960	2,935	3,788	3,696
Investments	14,857	15,803	14,882	19,530	19,667
Net Advances	40,908	44,800	48,581	52,195	58,033
<i>Growth</i>	<i>5%</i>	<i>10%</i>	<i>8%</i>	<i>7%</i>	<i>11%</i>
Other assets	1,697	2,029	2,181	2,399	2,567
<b>Total assets</b>	<b>61,808</b>	<b>66,929</b>	<b>69,340</b>	<b>80,324</b>	<b>86,225</b>

Asset Quality	FY17	FY18	FY19	FY20E	FY21E
GNPA	1,484	3,016	4,450	4,528	4,932
GNPA ratio	3.6%	6.6%	8.8%	8.3%	8.2%
NNPA	1,033	1,863	2,420	1,940	1,915
NNPA ratio	2.5%	4.2%	5.0%	3.7%	3.3%
PCR (Calculated)	30%	38%	46%	57%	61%
Credit Cost	1.7%	2.9%	2.9%	2.6%	2.0%

Balance Sheet Ratios	FY17	FY18	FY19	FY20E	FY21E
CD Ratio	76.2%	78.7%	81.1%	75.8%	78.5%
CASA	27.7%	29.1%	29.9%	28.2%	28.7%
CAR	12.5%	14.4%	16.0%	15.7%	15.4%
Tier - 1	11.9%	13.9%	14.3%	14.0%	13.7%

Valuation Ratios	FY17	FY18	FY19	FY20E	FY21E
P/E	5.8	12.0	21.7	15.9	6.8
P/BV	0.7	0.7	0.7	0.7	0.6
P/ABV	0.9	0.9	1.1	1.0	0.9

Source: Company, NBRR

## Karur Vysya Bank Ltd.

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