

Collection trend encouraging; credit cost to  
remain elevated**Rs33**

## Q2FY21 result review

## Banking

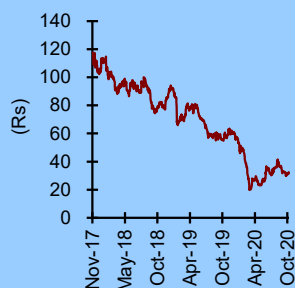
Target price: Rs33

## Shareholding pattern

	Mar '20	Jun '20	Sep '20
Promoters	2.1	2.1	2.1
Institutional investors	44.4	43.2	41.7
MFs and others	17.3	16.9	16.6
Insurance Cos.	0.2	0.1	0.1
FIs and Banks	4.4	4.2	3.3
FII	22.5	22.0	21.7
Others	53.5	54.7	56.2

Source: BSE

## Price chart



Karur Vysya Bank's (KVB) Q2FY21 earnings further improved to Rs1.15bn, taking multi-quarter high RoA to 0.63%, driven by strong NII growth at 7% QoQ and tight control on cost (up 5% QoQ). Management's prudent approach in utilising strong operating performance to beef up Covid-related contingency buffer (~45bps of loans) and improve coverage ratio to 64% would ensure lower earnings volatility going ahead. While asset quality improvement in Q2FY21 is not too relevant due to the Supreme Court's interim order, its GNPL ratio is steadily improving through past five quarters. Currently, GNPL ratio stands at 7.9% vs peak of 9.2% in Q1FY20. While we believe KVB's upgraded digital platform, cost optimisation drive, sharp improvement in coverage ratio over the past couple of years, may revive RoA to 0.7% by FY22E, lower contingency buffer poses risk to near term credit cost and growth. Maintain HOLD with an unchanged TP of Rs33.

- ▶ **Loan mix continued to tilt towards retail; incremental growth mainly driven by gold loans.** While the overall credit growth continued to remain subdued with total loans growing by mere 2% YoY, it showed early sign of revival with it growing 4% QoQ – highest sequential growth in past many quarters. Incremental growth in Q2FY21 was mainly driven by gold loan (up 12% QoQ), while rest of the segments continued to deliver sluggish sequential growth between 1-2%. Along with gold loans, home loans & personal loans too reported relatively higher sequential growth at 3% each. As a result, the share of retail loans further increased to 76% in Q2FY21 from 73% in Q2FY20.
- ▶ **Liability strength visible in strong CASA accretion.** While total deposit growth remaining muted at 2% QoQ, CASA accretion remained strong at 4% QoQ. Within CASA, CA growth remains higher at 4.5% QoQ while SA growth remains at 4% QoQ. As a result, CASA ratio further increases highest ever to 34% in Q2FY21. Strong retail liability franchise (~94% of term deposits in <Rs20mn bucket) and steady improvement in CASA helped it reduce its cost of deposit by 30bps QoQ. Margins expanded 11bps QoQ largely benefitting from lower cost of fund.
- ▶ **Digital journey remained on track:** Over the past couple of years, KVB has completely transformed its digital platform with most of its asset products already migrated to it. KVB initiated a second phase of transformation by realigning key business processes with the revamped platform. The same is likely to release ~540 staff (net decline in manpower by 72 in Q2FY21) and save Rs240mn (~4bps of total assets) in manpower costs.
- ▶ **Collection efficiency stands at ~95% of portfolio level.** While asset quality improvement is not too relevant due to the Supreme Court's interim order, collection efficiency at 90% in Morat book is suggesting better-than-expected portfolio behaviour. Management expects credit cost to remain between 1.55-2.5% in FY21E. It expects incremental restructuring of 2.5% from sectors like CRE, hospitality and textile etc.

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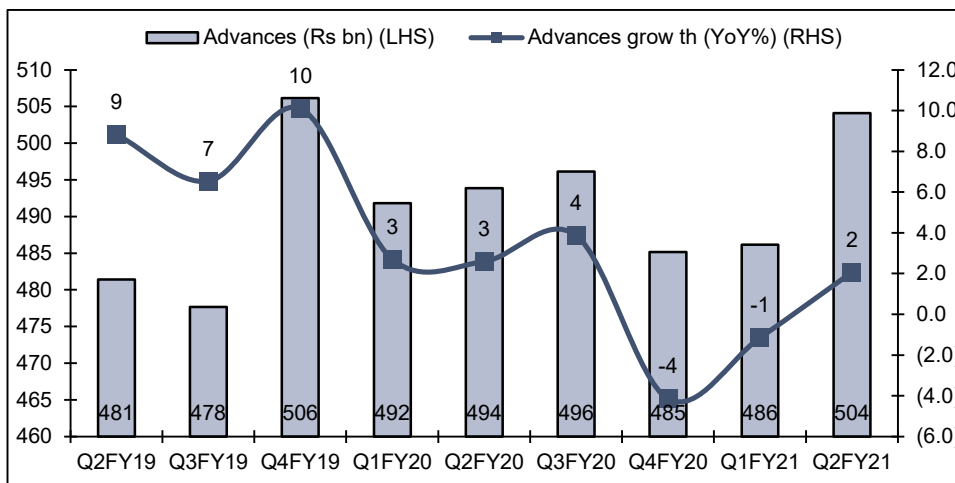
Market Cap	Rs25.7bn/US\$346mn	Year to Mar	FY19	FY20	FY21E	FY22E
Reuters/Bloomberg	KARU.BO/ KVB IN	NII (Rs bn)	23.6	23.5	23.5	26.0
Shares Outstanding (mn)	799.2	Net Profit (Rs bn)	2.1	2.4	4.2	5.3
52-week Range (Rs)	64/20	EPS (Rs)	2.8	2.9	5.2	6.6
Free Float (%)	97.9	% Chg YoY	-44.5	6.4	77.8	26.1
FII (%)	21.7	P/E (x)	11.7	11.0	6.2	4.9
Daily Volume (US\$'000)	1,203	P/BV (x)	0.4	0.4	0.4	0.3
Absolute Return 3m (%)	(6.9)	Net NPA (%)	4.9	3.9	6.1	4.6
Absolute Return 12m (%)	(41.9)	Dividend Yield (%)	1.1	4.1	0.0	4.0
Sensex Return 3m (%)	6.1	RoA (%)	0.3	0.3	0.6	0.7
Sensex Return 12m (%)	0.2	RoE (%)	3.3	3.6	6.2	7.3

**Table 1: Q2FY21 result review***(Rs mn)*

	Q2FY21	Q2FY20	% change YoY	Q1FY21	% change QoQ
Interest Income	13,947	15,375	(9.3)	13,761	1.4
Interest Expended	7,932	9,412	(15.7)	8,143	(2.6)
<b>Net interest income (NII)</b>	<b>6,015</b>	<b>5,963</b>	<b>0.9</b>	<b>5,618</b>	<b>7.1</b>
Other income	2,716	2,777	(2.2)	3,171	(14.4)
<b>Total income</b>	<b>8,731</b>	<b>8,740</b>	<b>(0.1)</b>	<b>8,790</b>	<b>(0.7)</b>
Operating expenses	4,243	4,429	(4.2)	4,051	4.7
-Staff expenses	2,206	2,130	3.5	2,136	3.2
-Other expenses	2,037	2,299	(11.4)	1,915	6.4
<b>Operating profit</b>	<b>4,488</b>	<b>4,312</b>	<b>4.1</b>	<b>4,739</b>	<b>(5.3)</b>
Total provisions	2,847	3,652	(22.0)	3,376	(15.7)
<b>Profit before tax</b>	<b>1,640</b>	<b>660</b>	<b>148.6</b>	<b>1,363</b>	<b>20.3</b>
Tax	491	27	1,747.4	308	59.5
<b>Profit after tax</b>	<b>1,149</b>	<b>633</b>	<b>81.4</b>	<b>1,055</b>	<b>8.9</b>
<b>Balance sheet (Rs mn)</b>					
Deposits	6,11,224	6,22,128	(1.8)	6,00,650	1.8
Advances	4,78,218	4,71,018	1.5	4,61,310	3.7
Gross NPL (Rs mn)	39,984	43,910	(8.9)	40,557	(1.4)
Net NPL (Rs mn)	14,282	21,184	(32.6)	15,852	(9.9)
<b>Ratios (%)</b>					
			<b>bps change</b>		<b>bps change</b>
<b>Profitability ratios</b>					
Yield on Advances	9.3	9.9	(59)	9.3	(6)
Cost of Funds	5.1	6.0	(86)	5.4	(33)
<b>NIM</b>	<b>3.5</b>	<b>3.5</b>	<b>1</b>	<b>3.4</b>	<b>11</b>
RoaA	0.6	0.3	29	0.6	4
RoaE	6.7	3.9	287	6.3	45
<b>Asset Quality</b>					
Gross NPL ratio	7.9	8.9	(96)	8.3	(41)
Net NPL ratio	3.0	4.5	(151)	3.4	(45)
Coverage ratio (Cal.)	64.3	51.8	1,252	60.9	337
<b>Business &amp; Other Ratios</b>					
Low-cost deposit mix	34.0	30.0	400	33.0	100
Cost-income ratio	48.6	50.7	(207)	46.1	251
Credit deposit ratio	78.2	75.7	253	76.8	144
CAR	18.4	15.9	251	18.1	27
Tier-I	16.4	14.3	210	16.1	22

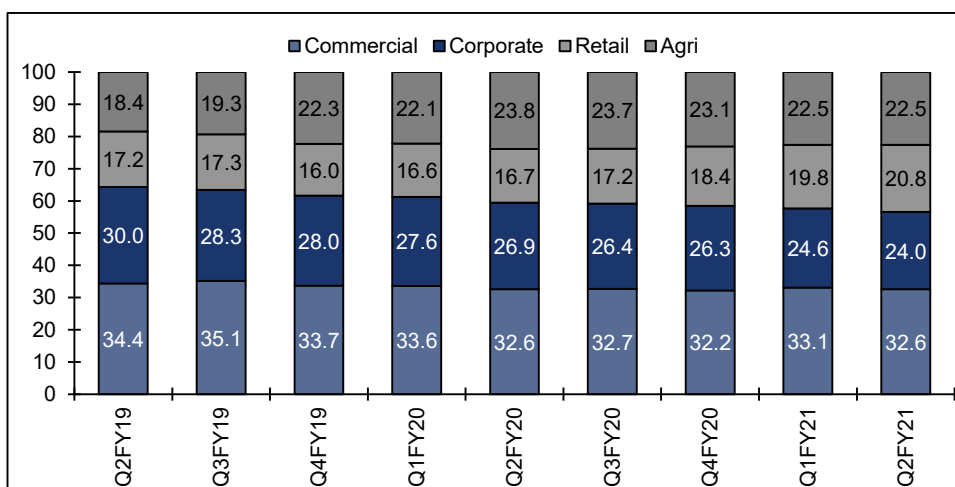
Source: Company, I-Sec research

**Chart 1: Overall advances fell 2% YoY; upgraded digital platform is likely to ensure sustainable long-term business growth**



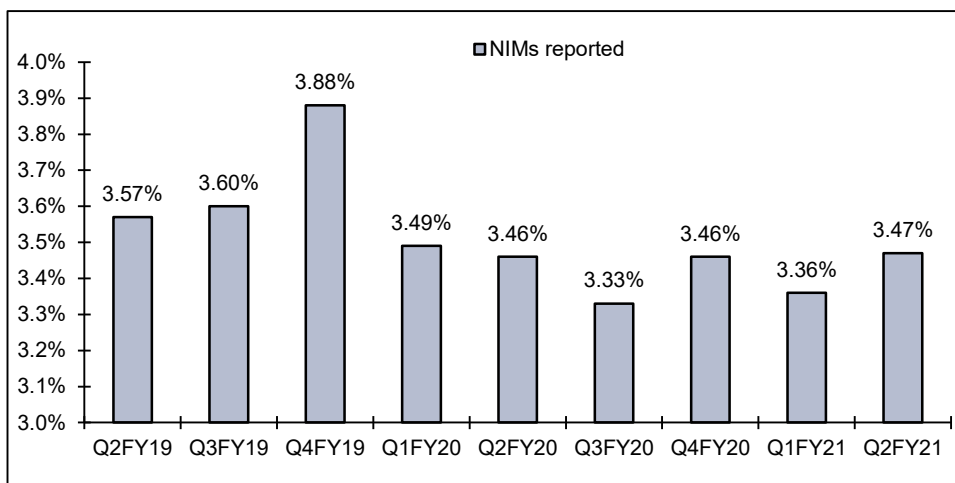
Source: Company, I-Sec research

**Chart 2: KVB continues to expand retail lending; corporate loan-book share now stands at 24% vs 27% in Q2FY20**



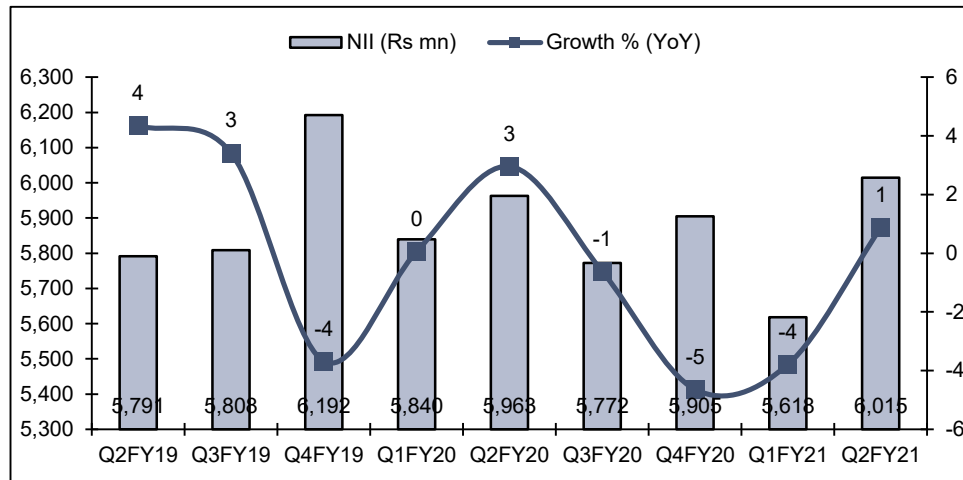
Source: Company, I-Sec research

**Chart 3: NIM expanded 11bps QoQ due to reduction in cost of deposits**



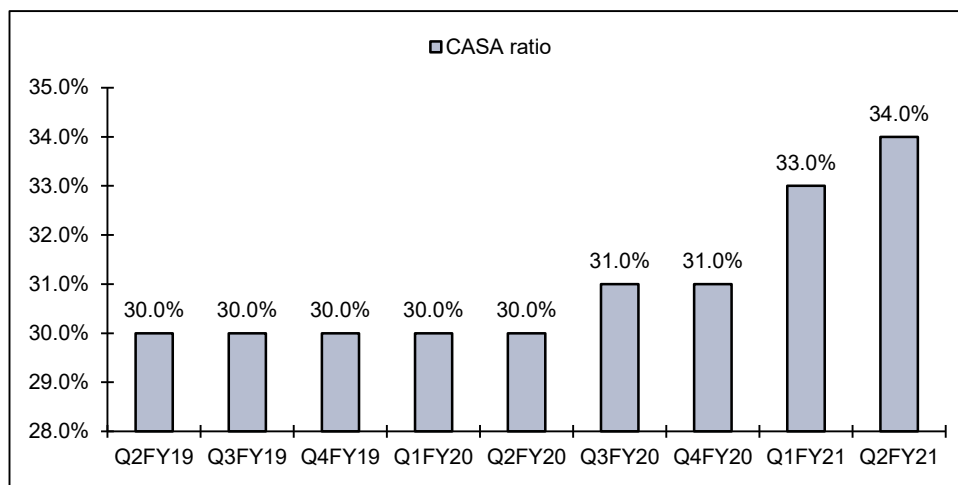
Source: Company, I-Sec research

**Chart 4: NII grew 1% YoY supported by NIM expansion**



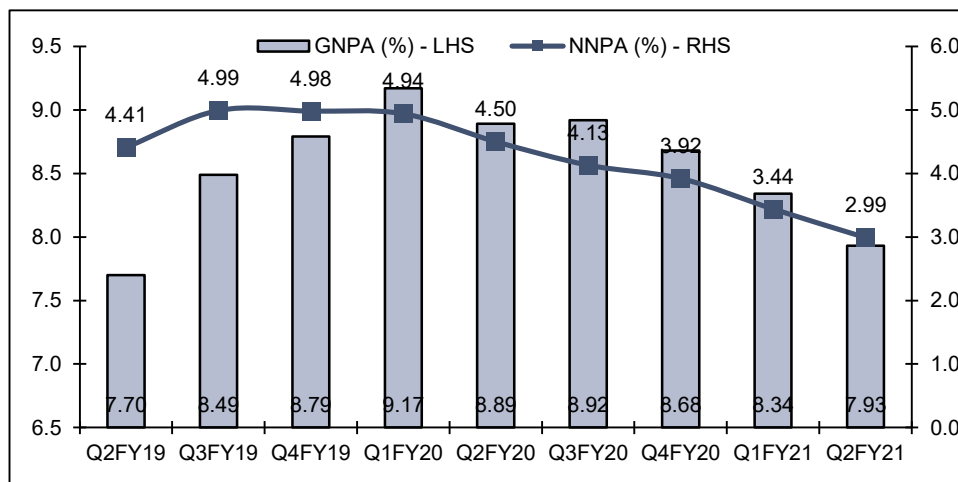
Source: Company, I-Sec research

**Chart 5: CASA ratio improves to 34%**



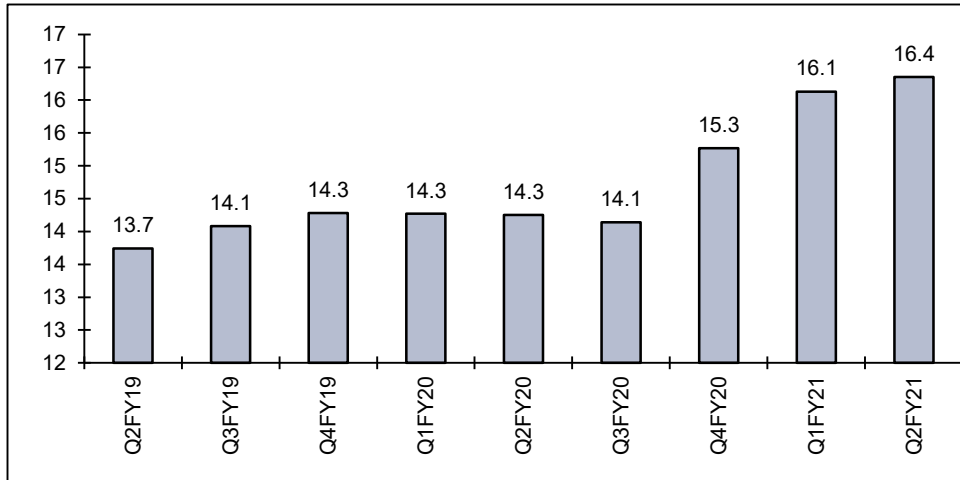
Source: Company, I-Sec research

**Chart 6: Asset quality improves**



Source: Company, I-Sec research

**Chart 7: Tier-1 ratio remained at 16.4%**



Source: Company, I-Sec research

## Financial summary

Table 2: Profit and loss statement

(Rs mn, year ending March 31)

	FY19	FY20	FY21E	FY22E
Interest Income	58,158	59,900	58,767	65,354
Interest Expense	34,530	36,420	35,312	39,328
<b>Net Interest Income</b>	<b>23,628</b>	<b>23,479</b>	<b>23,455</b>	<b>26,026</b>
% NII Growth	2.8	(0.6)	(0.1)	11.0
Treasury Income				
<b>Non-interest income</b>	<b>9,628</b>	<b>11,546</b>	<b>10,791</b>	<b>11,103</b>
<b>Net Revenue</b>	<b>33,256</b>	<b>35,026</b>	<b>34,246</b>	<b>37,129</b>
Employees Expenses	7,612	8,567	8,823	9,529
Other Op. Expenses	8,536	8,851	9,116	9,845
<b>Operating Profit</b>	<b>17,108</b>	<b>17,609</b>	<b>16,306</b>	<b>17,754</b>
% OP Growth	-3.7	2.9	-7.4	8.9
Tax	1,114	372	1,393	1,756
Total Provisions	13,886	14,887	10,736	10,731
<b>Net Profit</b>	<b>2,109</b>	<b>2,350</b>	<b>4,178</b>	<b>5,267</b>
% PAT Growth	(39.0)	11.5	77.8	26.1

Source: Company data, I-Sec research

Table 3: Balance sheet

(Rs mn, year ending March 31)

	FY19	FY20	FY21E	FY22E
Capital	1,599	1,599	1,599	1,599
Reserves and Surplus	62,629	64,404	68,195	72,263
Deposits	5,98,680	5,90,751	6,38,011	7,33,712
Borrowings	15,653	11,842	9,395	11,025
Other Liabilities & Provisions	14,840	14,186	4,033	13,068
<b>Total liabilities</b>	<b>6,93,402</b>	<b>6,82,782</b>	<b>7,21,233</b>	<b>8,31,667</b>
Cash & Balances with RBI	29,347	27,327	29,133	33,513
Bal. with banks/ call money	7,624	16,599	12,347	17,927
Investment	1,48,816	1,57,624	1,59,503	1,83,428
Loans and advances	4,85,808	4,60,981	4,97,860	5,72,539
Fixed Assets	5,830	5,866	6,280	6,861
Other Assets	15,977	14,384	16,110	17,399
<b>Total assets</b>	<b>6,93,401</b>	<b>6,82,782</b>	<b>7,21,233</b>	<b>8,31,667</b>
% TA Growth	4	(2)	6	15

Source: Company data, I-Sec research

Table 4: Key ratios

(Year ending March 31)

	FY19	FY20	FY21E	FY22E
<b>Per Share Data</b>				
Book value per share (INR)	80.3	82.6	87.3	92.4
Adj. BVPS (INR)	57.6	65.6	59.0	67.7
<b>Price/Book value</b>	<b>0.40</b>	<b>0.39</b>	<b>0.4</b>	<b>0.3</b>
<b>Price/ Adj. Book value</b>	<b>0.6</b>	<b>0.5</b>	<b>0.5</b>	<b>0.5</b>
EPS(INR)	2.8	2.9	5.2	6.6
<b>P/E Ratio</b>	<b>11.7</b>	<b>11.0</b>	<b>6.2</b>	<b>4.9</b>
<b>DPS</b>	2.8	1.3	-	1.3
<b>Asset Quality</b>				
Gross NPA (Rs mn)	44,498	42,128	51,354	43,881
Gross NPA (%)	8.79	8.68	10.31	7.66
Net NPA (Rs mn)	24,203	18,087	30,222	26,307
Net NPA (%)	4.98	3.92	6.07	4.59
% coverage of NPA	45.6	57.1	41.2	40.1
Delinquencies (%)	5.0	3.4	5.0	2.3

Capital Adequacy Ratios

RWA (Rs mn)	4,37,325	4,14,976	4,48,174	5,15,400
<b>Tier 1 (%)</b>	<b>14.3</b>	<b>15.3</b>	<b>15.2</b>	<b>14.0</b>
Tier 2 (%)	1.7	1.9	1.8	1.5
<b>Total CAR (%)</b>	<b>16.0</b>	<b>17.2</b>	<b>17.0</b>	<b>15.6</b>

Business Ratios

Credit / Deposit(%)	81.1	78.0	78.0	78.0
Investment / Deposit (%)	24.9	26.7	25.0	25.0
<b>CASA (%)</b>	<b>29.9</b>	<b>31.3</b>	<b>27.8</b>	<b>27.8</b>
<b>RoA (%)</b>	<b>0.3</b>	<b>0.3</b>	<b>0.6</b>	<b>0.7</b>
Core RoE (%)	3.3	3.6	6.2	7.3
Dividend Yield (%)	8.5%	4.1%	0.0%	4.1%

Earnings Ratios

Interest Inc. / Avg. assets (%)	8.5	8.7	8.4	8.4
Interest Exp./ Avg. assets (%)	5.1	5.3	5.0	5.1
<b>NIM (%)</b>	<b>3.5</b>	<b>3.4</b>	<b>3.3</b>	<b>3.4</b>
Int. exp/ Int earned (%)	59.4	60.8	60.1	60.2
Oth. Inc./ Tot. Inc. (%)	29.0	33.0	31.5	29.9
Staff exp/Total opt. exp (%)	47.1	49.2	49.2	49.2
<b>Cost/ Income Ratio (%)</b>	<b>48.6</b>	<b>49.7</b>	<b>52.4</b>	<b>52.2</b>
Prov./ Operating Profit (%)	81.2	84.5	65.8	60.4
<b>Loan loss prov./Avg. loans (bps)</b>	<b>297.4</b>	<b>314.5</b>	<b>223.9</b>	<b>200.5</b>

Source: Company data, I-Sec research

Table 5: RoA tree

(% , year ending March 31)

	FY19	FY20	FY21E	FY22E
Interest income/Assets	8.5	8.7	8.4	8.4
Interest expenses/Assets	5.1	5.3	5.0	5.1
<b>Net interest income/Assets</b>	<b>3.5</b>	<b>3.4</b>	<b>3.3</b>	<b>3.4</b>
Other Inc. from operations/Assets	1.4	1.7	1.5	1.4
Total income/Assets	4.9	5.1	4.9	4.8
Employee expenses/Assets	1.1	1.2	1.3	1.2
Other operating expenses/Assets	1.3	1.3	1.3	1.3
<b>Total Opex</b>	<b>2.4</b>	<b>2.5</b>	<b>2.6</b>	<b>2.5</b>
<b>Operating profit/Assets</b>	<b>2.5</b>	<b>2.6</b>	<b>2.3</b>	<b>2.3</b>
Tax/Assets	0.2	0.1	0.2	0.2
Loan loss provisions/Assets	2.0	2.2	1.5	1.4
<b>Net profit/Assets</b>	<b>0.3</b>	<b>0.3</b>	<b>0.6</b>	<b>0.7</b>

Source: Company data, I-Sec research

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