

Karur Vysya Bank

Performance Highlights

| Particulars (₹ cr) | 1QFY18 | 4QFY17 | % chg (qoq) | 1QFY17 | % chg (yoy) |
|--------------------|------------|------------|-------------|------------|-------------|
| NII | 539 | 580 | (7) | 481 | 12 |
| Pre-prov. profit | 449 | 508 | (12) | 283 | 59 |
| PAT | 148 | 219 | (32) | 146 | 1 |

Source: Company, Angel Research

KVB's 1QFY18 results were in line with expectations. While PAT remained flat YoY and loan growth remained 7.7%, overall growth should pick in 2HFY18. While slippages were high during the quarter, they were largely from the watch list. Next two quarters could be challenging, but FY19 looks much stronger for the bank.

Loan continued to be in single digit; however the management commentary remains positive: For FY17 KVB had a muted loan growth of 4.7% and the management had indicated at pick up in credit growth in FY18. Growth for 1QFY18 too remained tepid at 7.7%. Loan to corporate grew by 4%, while retail loans had a decent growth of 10%. However, the management remains confident of achieving double digit growth in FY18, which we believe is doable. We have factored in 10%/12% growth in advances for FY18/19 respectively.

Deposit growth has been in sync with loan growth: Overall deposits grew by 7.8% which is in sync with the growth in loan book. However, the CASA growth continued to outpace the overall growth, up 29.4% and accordingly the CASA ratio has improved further to 29.2% vs 27.7% QoQ. KVB had seen a 590 bps jump in its CASA base post demonetization; though there were some outflows in the deposits subsequently, overall CASA ratio remains fairly strong.

Slippages remained elevated, however were largely from the watch list: Slippages during the quarter stood at ₹ 389 cr, though it was lower than ₹ 560 cr in Q4FY17, overall it remained elevated. During the quarter one large account slipped from the watch list and few more accounts remain under stress. At the end of Q4FY17 the management had indicated at around ₹ 650 cr under watch list and with the one large account slipping into NPA, the watch list is down to ₹ 450 cr. On QoQ basis GNPA's & NNPA's went up 69 bps and 32 bps to 4.27% and 2.85%. With recovery process gaining steam we expect overall GNPA's to be under control.

Outlook and valuation: While credit cost will still remain elevated in FY18, we expect FY19 to be a more meaningful year for the bank with RoE improving to 14.7% from 12.6% in FY17. Despite the recent run up, the stock is trading at 1.6x its FY19 Adj BV, and we believe this leaves further scope for re-rating. **We maintain ACCUMULATE on the stock with a target price of ₹ 160.**

Key financials (standalone)

| Y/E March (₹ cr) | FY2016 | FY2017 | FY2018E | FY2019E |
|-------------------|--------------|--------------|--------------|--------------|
| NII | 1,781 | 2,074 | 2,388 | 2,757 |
| % chg | 21.5 | 16.4 | 15.1 | 15.4 |
| Net profit | 568 | 607 | 660 | 858 |
| % chg | 24.7 | 6.9 | 8.8 | 29.9 |
| NIM (%) | 3.2 | 3.5 | 3.7 | 3.9 |
| EPS (₹) | 9.3 | 10.0 | 10.8 | 14.1 |
| P/E (x) | 15.0 | 14.1 | 12.9 | 9.9 |
| P/ABV (x) | 2.0 | 2.1 | 1.9 | 1.6 |
| RoA (%) | 1.0 | 1.0 | 1.0 | 1.2 |
| RoE (%) | 12.9 | 12.6 | 12.5 | 14.7 |

Source: Company, Angel Research; Note: CMP as of August 04, 2017

ACCUMULATE

| | |
|--------------|-------|
| CMP | ₹ 140 |
| Target Price | ₹ 160 |

| | |
|-------------------|-----------|
| Investment Period | 12 months |
|-------------------|-----------|

Stock Info

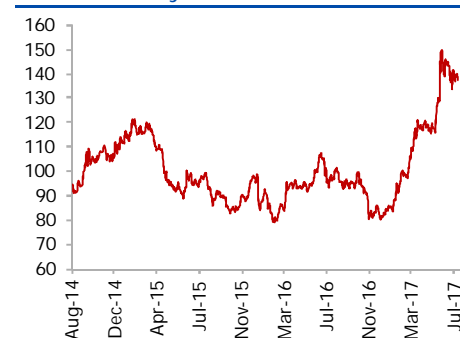
| | |
|--------------------|----------|
| Sector | Banks |
| Market Cap (₹ cr) | 8,530 |
| Beta | 0.7 |
| 52 Week High / Low | 153/80 |
| Avg. Daily Volume | 1,11,269 |
| Face Value (₹) | 2 |
| BSE Sensex | 32,325 |
| Nifty | 10,066 |
| Reuters Code | KARU.BO |
| Bloomberg Code | KVB@IN |

Shareholding Pattern (%)

| | |
|-------------------------|------|
| Promoters | 2.1 |
| MF / Banks / Indian FIs | 30.4 |
| FII / NRIs / OCBs | 21.0 |
| Indian Public / Others | 46.5 |

| Abs.(%) | 3m | 1yr | 3yr |
|---------|------|------|------|
| Sensex | 8.5 | 16.1 | 26.3 |
| KVB | 16.0 | 44.0 | 49.0 |

3- Year Daily Price Chart



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Exhibit 1: Income Statement (Quarterly)

| Particulars (₹ cr) | Q3FY16 | Q4FY16 | Q1FY17 | Q2FY17 | Q3FY17 | Q4FY17 | Q1FY18 | % YoY | % QoQ |
|----------------------------|------------|------------|------------|------------|------------|------------|------------|--------------|-------------|
| Interest earned | 1,352 | 1,370 | 1,385 | 1,393 | 1,411 | 1,433 | 1,384 | (0.1) | (3) |
| Interest expenses | 904 | 898 | 904 | 898 | 894 | 853 | 846 | (6.5) | (1) |
| Net interest income | 448 | 473 | 481 | 495 | 518 | 580 | 539 | 11.9 | (7) |
| Non Interest Income | 173 | 166 | 162 | 218 | 170 | 233 | 236 | 45.7 | 1.3 |
| Operating income | 621 | 639 | 643 | 713 | 688 | 813 | 775 | 20.4 | (5) |
| Operating expenses | 295 | 380 | 360 | 393 | 416 | 305 | 325 | (9.7) | 6.7 |
| Pre-prov. profit | 326 | 259 | 283 | 320 | 272 | 508 | 449 | 58.8 | (12) |
| Provisions & cont. | 93 | -13 | 67 | 119 | 94 | 218 | 233 | 248.8 | 7.3 |
| PBT | 233 | 271 | 216 | 200 | 178 | 291 | 216 | (0.1) | (26) |
| Prov. for taxes | 80 | 134 | 70 | 74 | 62 | 72 | 68 | (2.5) | (5.6) |
| PAT | 153 | 138 | 146 | 126 | 116 | 219 | 148 | 1.1 | (32) |
| EPS (₹) | 2.5 | 2.3 | 2.4 | 2.1 | 1.9 | 3.6 | 2.4 | 1.1 | (32.4) |
| Effective tax rate (%) | 34.4 | 49.2 | 32.3 | 36.9 | 34.8 | 24.8 | 31.5 | (2.4) | 27 |

Source: Company, Angel Research

Exhibit 2: Loan Break Up & Growth (%)

| Advances Break Up | Q4FY16 | Q1FY17 | Q2FY17 | Q3FY17 | Q4FY17 | Q1FY18 |
|--------------------------|--------|--------|--------|--------|--------|--------|
| Commercial | 32% | 33% | 34% | 34% | 33% | 34% |
| Agriculture | 18% | 18% | 18% | 17% | 17% | 18% |
| Retail | 15% | 15% | 16% | 16% | 15% | 16% |
| Corporate | 35% | 34% | 33% | 34% | 35% | 32% |
| Advances Growth Break Up | | | | | | |
| Total Advances | 7.6% | 5.8% | 5.4% | 1.6% | 5.0% | 7.7% |
| Commercial | 8.4% | 9.5% | 9.4% | 7.0% | 6.7% | 11.7% |
| Agriculture | 12.7% | 12.0% | 10.2% | 3.1% | -0.8% | 5.1% |
| Retail | 12.2% | 11.5% | 11.4% | 7.4% | 7.1% | 9.7% |
| Corporate | 2.7% | -2.6% | -3.0% | -6.4% | 5.4% | 4.2% |

Source: Company, Angel Research

Exhibit 3: Loan Book Break Up (₹ Cr)

| Loan Book Composition | Q1FY17 | Q2FY17 | Q3FY17 | Q4FY17 | Q1FY18 |
|-----------------------|---------------|---------------|---------------|---------------|---------------|
| Total Advances | 39,381 | 39,537 | 38,460 | 41,435 | 42,401 |
| Commercial | 12,905 | 13,303 | 13,035 | 13,612 | 14,411 |
| Agriculture | 7,265 | 6,950 | 6,442 | 6,979 | 7,635 |
| Retail | 6,009 | 6,170 | 6,093 | 6,340 | 6,592 |
| Corporate | 13,202 | 13,114 | 12,890 | 14,504 | 13,763 |

Source: Company, Angel Research

Loan growth continued to be in single digit; however the management commentary remains positive: For FY17 KVB had a muted loan growth of 4.7% and the management had indicated at pick up in credit growth in FY18. Growth for 1QFY18 too remained tepid at 7.7%. Loan to corporate grew by 4%, while retail loans had a decent growth of 10%. However, the management remains confident of achieving double digit growth in FY18, which we believe is doable. We have factored in 10% /12% growth in advances for FY18 /19 respectively. The management had earlier expected a 15% growth in FY18; however, given the lack of overall credit demand we believe 10-12% would be more realistic for the bank.

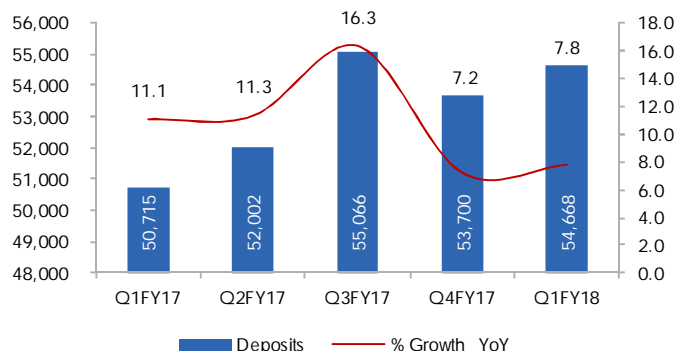
Deposit growth has been in sync with loan growth: Overall deposits grew by 7.8% which is in sync with the growth in loan book. However, the CASA growth continued to outpace the overall growth, up 29.4% and accordingly the CASA ratio has improved further to 29.2% vs 27.7% QoQ. KVB had seen a 590 bps jump in its CASA base post demonetization; though there were some outflows in the deposits subsequently the overall CASA ratio remains fairly strong.

Exhibit 4: Loan growth momentum was strong



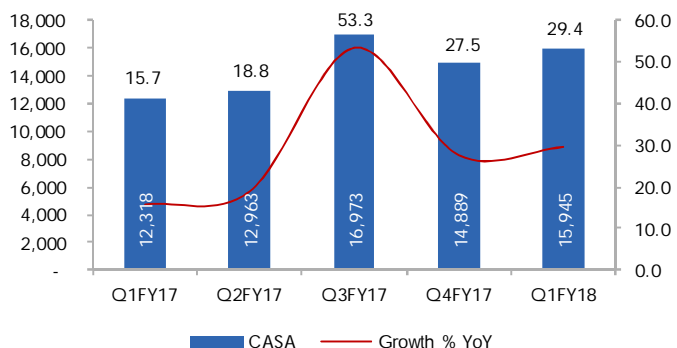
Source: Company, Angel Research

Exhibit 5: Deposit growth also remained strong



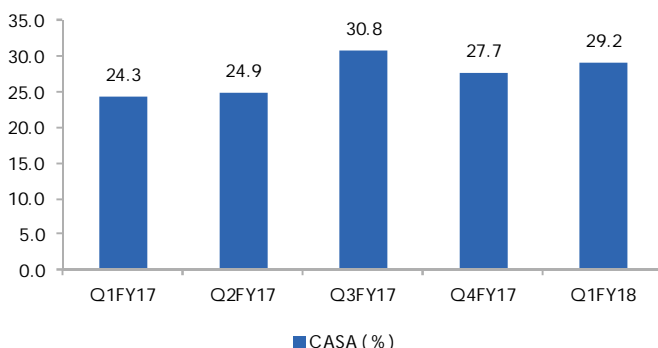
Source: Company, Angel Research

Exhibit 6: CASA Growth strong as well



Source: Company, Angel Research

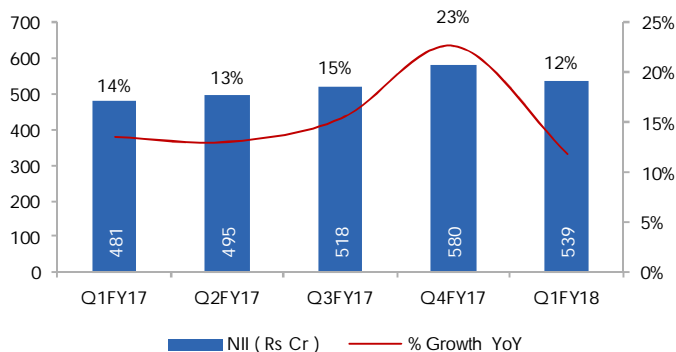
Exhibit 7: CASA Ratio has improved further (%)



Source: Company, Angel Research

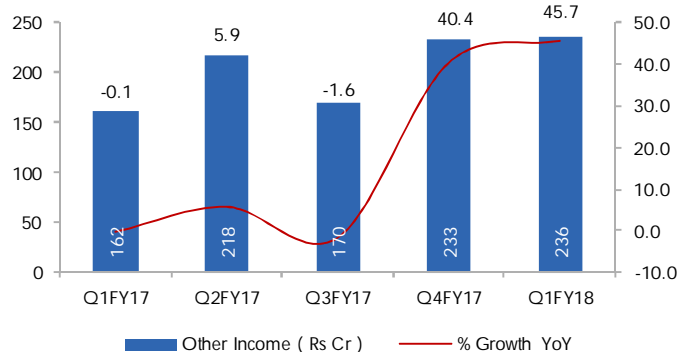
Higher provisions dented profit growth: Higher slippages and consequent interest reversal impacted the NII growth during the quarter, which stood at 12% YoY. This was much lower than the 23% YoY growth seen in Q4FY17. As we have mentioned earlier the slippages could remain higher in the Q2FY18 as well and could come down in the 2HFY18, hence we expect pick up in NII growth during the 2nd half of the financial year.

Exhibit 8: NII Growth (%)



Source: Company, Angel Research

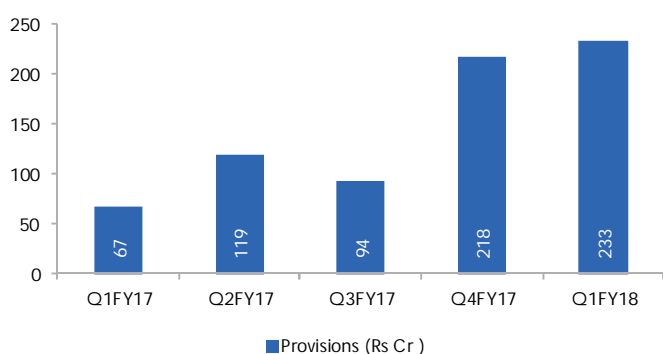
Exhibit 9: Other income boosted backed by fees (₹ Cr)



Source: Company, Angel Research

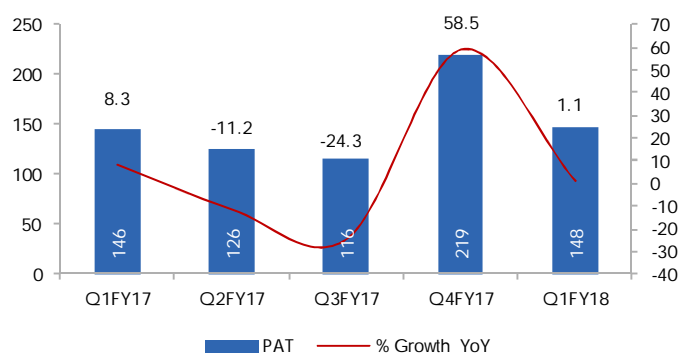
Other income of the bank has remained strong for the Q4FY17 as well as Q1FY18, due to higher transactions and ATM related fees. While overall growth in the fee income could moderate as more and more ATMs of other banks starts operating, the growth would still be higher than FY17. Provisions during the quarter higher than expected and hence PAT remained flat YoY.

Exhibit 10: Provisions were higher (₹ Cr)



Source: Company, Angel Research

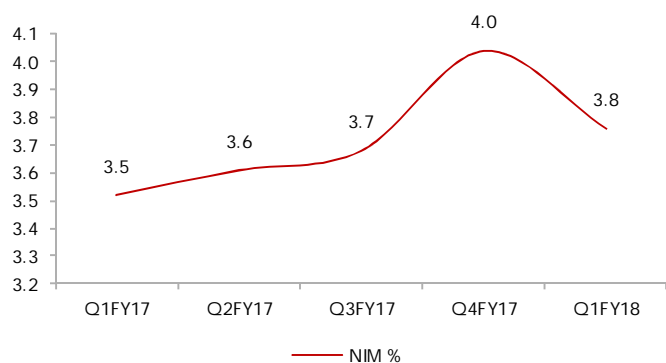
Exhibit 11: PAT impacted by higher provisions (₹ Cr)



Source: Company, Angel Research

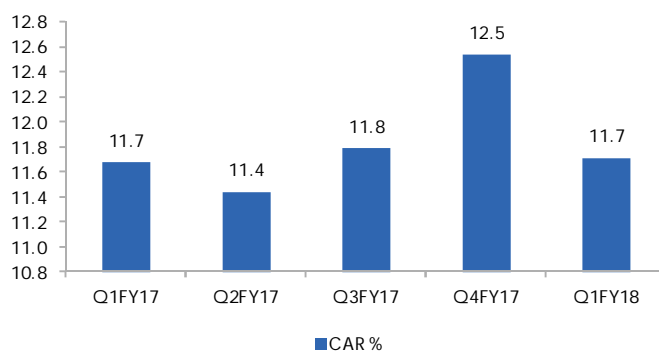
NIM declined due to higher slippages and consequent interest reversal; In the FY17 the bank had witnessed steady rise in NIM, backed by lower cost of funds. Increasing share of CASA had been instrumental in helping lower cost of funds and better NIM. However, during the quarter the bank witnessed one large slippages and the interest reversal had a negative impact on the NIM.

Exhibit 12: NIM declined due to higher slippages



Source: Company, Angel Research

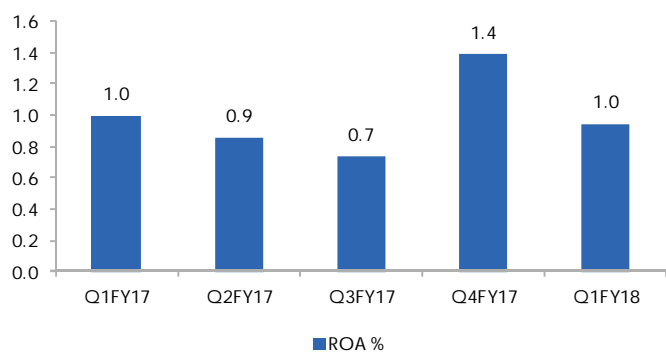
Exhibit 13: Capital raising planned in near term (%)



Source: Company, Angel Research

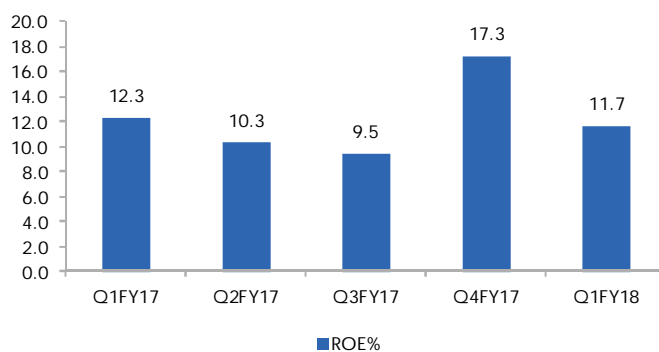
The RoA and RoE of the bank which had started showing positive trend again under pressure during the quarter, due to higher than expected provisions. However, the management remains confident that the slippages and consequent provisions will be lower in the 2HFY18, and this should help in normalizing of return ratios. Further the bank is in the process of raising capital to meet the incremental expected growth in FY19 and higher growth coupled with strong traction in fee income should lift the return ratios in FY19.

Exhibit 14: RoA Trend (%)



Source: Company, Angel Research

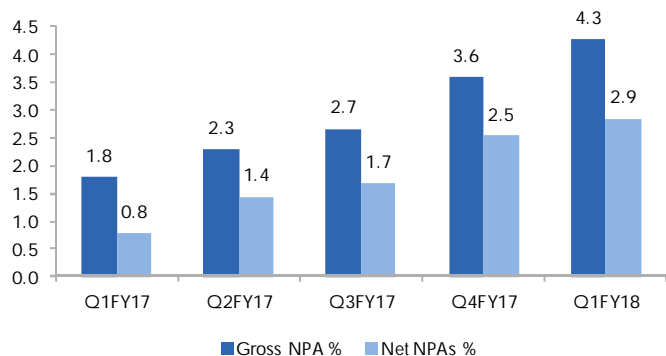
Exhibit 15: ROE Trend (%)



Source: Company, Angel Research

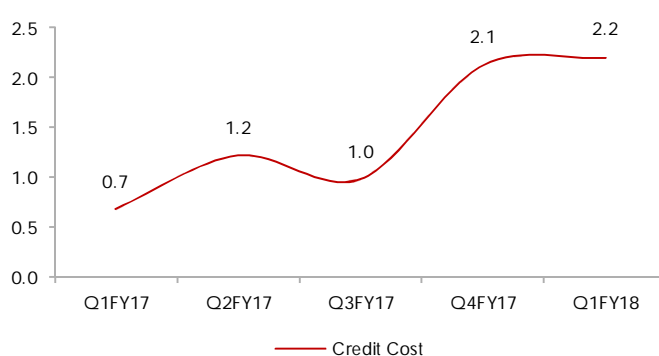
Slippages remained elevated, however were largely from the watch list: Slippages during the quarter stood at ` 389 cr, though it was lower than ` 560 cr in Q4FY17, overall it remained elevated. During the quarter one large account slipped from the watch list and few more accounts remain under stress. At the end of Q4FY17 the management had indicated at around ` 650 cr under watch list and with the one large account slipping into NPA, the watch list is down to ` 450 cr. On QoQ basis GNPA's & NNPA's went up 69 bps and 32 bps to 4.27% and 2.85%. With recovery process gaining steam we expect overall GNPA's to be under control.

Exhibit 16: Asset quality weakened QoQ (%)



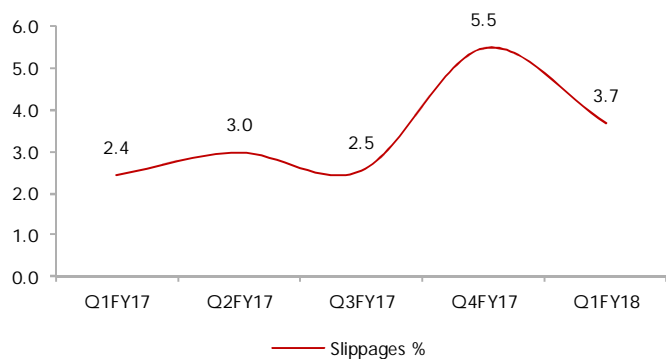
Source: Company, Angel Research

Exhibit 17: Credit Cost (%)



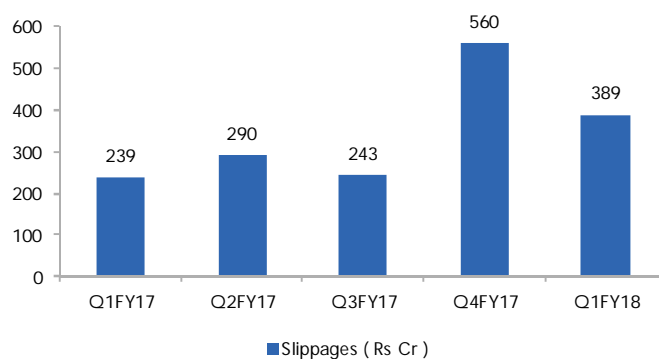
Source: Company, Angel Research

Exhibit 18: Slippages Ratios (%)



Source: Company, Angel Research

Exhibit 19: Slippages increased (` cr)



Source: Company, Angel Research

Outlook and valuation

While credit cost will still remain elevated in FY18, we expect FY19 to be a more meaningful year for the bank. In order to meet higher growth in the years to come the bank is also in the process of raising capital. The fee income of the bank has gained momentum and with cost remaining under control we expect RoE to improve to 14.7% from 12.6% in FY17. Despite the recent run up, the stock is trading at 1.6x its FY19 Adj BV, which we believe leaves further scope for re-rating. **We maintain ACCUMULATE on the stock with a target price of ₹ 160.**

Exhibit 20: Income Statement

| Y/E March (₹ cr) | FY15 | FY16 | FY17 | FY18E | FY19E |
|-------------------------------|--------------|--------------|--------------|--------------|--------------|
| Net Interest Income | 1,466 | 1,781 | 2,074 | 2,388 | 2,757 |
| - YoY Growth (%) | 14.2 | 21.5 | 16.4 | 15.1 | 15.4 |
| Other Income | 581 | 707 | 783 | 902 | 874 |
| - YoY Growth (%) | 2.9 | 21.7 | 10.8 | 15.2 | (3.1) |
| Operating Income | 2,046 | 2,488 | 2,857 | 3,289 | 3,630 |
| - YoY Growth (%) | 10.7 | 21.6 | 14.8 | 15.1 | 10.4 |
| Operating Expenses | 1,103 | 1,253 | 1,475 | 1,648 | 1,827 |
| - YoY Growth (%) | 9.2 | 13.5 | 17.7 | 11.8 | 10.9 |
| Pre - Provision Profit | 943 | 1235 | 1382 | 1,641 | 1,803 |
| - YoY Growth (%) | 12.6 | 31.0 | 11.9 | 18.8 | 9.9 |
| Prov. & Cont. | 481 | 324 | 498 | 656 | 523 |
| - YoY Growth (%) | 8.6 | (32.6) | 53.8 | 31.8 | (20.3) |
| Profit Before Tax | 462 | 912 | 884 | 985 | 1280 |
| - YoY Growth (%) | 17.0 | 97.1 | (3.0) | 11.4 | 29.9 |
| Prov. for Taxation | 7 | 344 | 278 | 325 | 422 |
| - as a % of PBT | 1.6 | 37.7 | 31.4 | 33.0 | 33.0 |
| PAT | 455 | 568 | 607 | 660 | 858 |
| - YoY Growth (%) | 6.0 | 24.7 | 6.9 | 8.8 | 29.9 |

Source: Company, Angel Research

Exhibit 21: Balance Sheet

| Y/E March (₹ cr) | FY15 | FY16 | FY17 | FY18E | FY19E |
|--------------------------|---------------|---------------|---------------|---------------|---------------|
| Share Capital | 122 | 122 | 122 | 122 | 122 |
| Reserves & Surplus | 4,124 | 4,451 | 4,914 | 5,396 | 6,061 |
| Net worth | 4,246 | 4,573 | 5,036 | 5,518 | 6,183 |
| Deposits | 44,690 | 50,079 | 53,700 | 57,996 | 63,795 |
| - Growth (%) | 2.1 | 12.1 | 7.2 | 8.0 | 10.0 |
| Borrowings | 2,901 | 1,573 | 1,696 | 1,740 | 1,914 |
| - Growth (%) | (11.9) | (45.8) | 7.8 | 2.6 | 10.0 |
| Other Liab & Prov. | 1,315 | 1,439 | 1,376 | 1,450 | 1,595 |
| Total Liabilities | 53,152 | 57,664 | 61,808 | 66,703 | 73,487 |
| Cash balances | 2,693 | 2,529 | 2,790 | 2,900 | 3,190 |
| Bank balances | 56 | 263 | 1,555 | 580 | 638 |
| Investments | 12,773 | 13,222 | 14,857 | 16,239 | 17,863 |
| Advances | 36,109 | 39,084 | 40,908 | 44,998 | 50,398 |
| - Growth (%) | 6.2 | 8.2 | 4.7 | 10.0 | 12.0 |
| Fixed Assets | 411 | 420 | 419 | 470 | 517 |
| Other Assets | 1,110 | 2,146 | 1,279 | 1,516 | 881 |
| Total Assets | 53,152 | 57,664 | 61,808 | 66,703 | 73,487 |

Source: Company, Angel Research

Exhibit 22: Key Ratios

| Y/E March | FY15 | FY16 | FY17 | FY18E | FY19E |
|---------------------------------|-------------|-------------|-------------|-------------|-------------|
| Profitability Ratios (%) | | | | | |
| NIMs | 2.8 | 3.2 | 3.5 | 3.7 | 3.9 |
| Cost to Income Ratio | 53.9 | 50.3 | 51.6 | 50.1 | 50.3 |
| RoA | 0.9 | 1.0 | 1.0 | 1.0 | 1.2 |
| RoE | 12.0 | 12.9 | 12.6 | 12.5 | 14.7 |
| B/S ratios (%) | | | | | |
| CASA Ratio | 22.0 | 23.3 | 32.6 | 30.0 | 30.0 |
| Credit/Deposit Ratio | 80.8 | 78.0 | 76.2 | 77.6 | 79.0 |
| CAR | 14.6 | 12.2 | 12.5 | 12.8 | 13.1 |
| - Tier I | 13.6 | 11.3 | 11.7 | 12.0 | 12.3 |
| Asset Quality (%) | | | | | |
| Gross NPAs | 1.9 | 1.30 | 3.6 | 4.0 | 3.7 |
| Net NPAs | 0.8 | 0.6 | 2.5 | 2.5 | 1.9 |
| Slippages | 1.8 | 3.1 | 3.4 | 2.5 | 1.5 |
| Loan Loss Prov./Avg. Assets | 1.3 | 0.8 | 1.2 | 1.4 | 1.0 |
| Provision Coverage | 59 | 58 | 30 | 50 | 50 |
| Per Share Data (₹) | | | | | |
| EPS | 7.5 | 9.3 | 10.0 | 10.8 | 14.1 |
| BVPS | 69.8 | 75.0 | 82.6 | 90.6 | 101.5 |
| ABVPS | 65.2 | 71.5 | 65.7 | 75.1 | 85.7 |
| DPS | 1.0 | 3.0 | 2.0 | 3.0 | 4.0 |
| Valuation Ratios | | | | | |
| PER (x) | 18.7 | 15.0 | 14.1 | 12.9 | 9.9 |
| P/BVPS(x) | 2.0 | 1.9 | 1.7 | 1.5 | 1.4 |
| P/ABVPS (x) | 2.1 | 2.0 | 2.1 | 1.9 | 1.6 |
| Dividend Yield | 0.7 | 2.1 | 1.4 | 2.1 | 2.9 |
| DuPont Analysis (%) | | | | | |
| Interest Income | 10.3 | 9.8 | 9.4 | 9.4 | 9.6 |
| Interest Expenses | 7.5 | 6.6 | 5.9 | 5.7 | 5.6 |
| NII | 2.8 | 3.2 | 3.5 | 3.7 | 3.9 |
| Non Interest Income | 1.1 | 1.3 | 1.3 | 1.4 | 1.2 |
| Total Revenues | 3.9 | 4.5 | 4.8 | 5.1 | 5.2 |
| Operating Cost | 2.1 | 2.3 | 2.5 | 2.6 | 2.6 |
| PPP | 1.8 | 2.2 | 2.3 | 2.6 | 2.6 |
| Total Provisions | 0.9 | 0.6 | 0.8 | 1.0 | 0.7 |
| PreTax Profit | 0.9 | 1.6 | 1.5 | 1.5 | 1.8 |
| Tax | 0.0 | 0.6 | 0.5 | 0.5 | 0.6 |
| ROA | 0.9 | 1.0 | 1.0 | 1.0 | 1.2 |
| Leverage | 13.8 | 12.6 | 12.4 | 12.2 | 12.0 |
| RoE (%) | 12.0 | 12.9 | 12.6 | 12.5 | 14.7 |

Source: Company, Angel Research

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|---|-----------------------|--|---|
| Disclosure of Interest Statement | Karur Vysya Bank | | |
| 1. Financial interest of research analyst or Angel or his Associate or his relative | No | | |
| 2. Ownership of 1% or more of the stock by research analyst or Angel or associates or relatives | No | | |
| 3. Served as an officer, director or employee of the company covered under Research | No | | |
| 4. Broking relationship with company covered under Research | No | | |
| Ratings (Based on expected returns over 12 months investment period): | Buy (> 15%) | Accumulate (5% to 15%) Reduce (-5% to -15%) | Neutral (-5 to 5%) Sell (< -15) |