

Asset quality improves

KVB's Q2FY13 bottomline performance came in slightly below expectation (PAT at Rs1.3bn, up 17% YoY) though net total income was in line. A healthy 25bps NIM expansion QoQ and ~30bps improvement in %GNPA surprised us positively. Overall asset quality remains robust with slippages at ~1.0% and PCR healthy at ~75%. The restructured portfolio increased by 9% QoQ though it remains comfortable at 2.8%. We maintain our positive stance on the stock and our Buy recommendation with a revised target price of Rs550 (1.75x FY14E).

- **NIM expands 25bps QoQ:** NII grew by a strong 32% YoY to Rs2.9bn led by a smart 25bps expansion in NIM coupled with healthy credit growth (27% YoY). The NIM expansion can be traced to 25bps improvement in cost of deposits. We expect the NIM to stabilise at current levels for H2FY13.
- **GNPA improves sequentially:** Asset quality matrices continued to remain healthy with 1) GNPA improving by ~30 bps QoQ 2) PCR stable at 75% 3) and slippage rate contained at ~1.0%. Meanwhile, the restructured portfolio was up 9% sequentially though remaining comfortable at 2.8% of loans. KVB upgraded a textile exposure (Rs500mn exposure, had slipped in previous quarter) after restructuring it under CDR. This helped the bank write back the provisions created on the account. The management has stepped up monitoring and recovery efforts lately given the challenging economic environment.

Y/E March (Rsmn)	Q2FY13	Q2FY12	% YoY	Q1FY13	Q2FY13E	Var %
Net Interest Income	2,858	2,165	32.0	2,539	2,620	9.1
Non-Interest Income	850	747	13.8	1,043	1,057	(19.6)
Net Total Income	3,708	2,912	27.3	3,582	3,677	0.8
Operating Exp	1,765	1,335	32.2	1,555	1,579	11.8
Pre-Prov. Profit	1,943	1,577	23.2	2,027	2,098	(7.4)
Provisions	(206)	133	-	(100)	212	-
Profit Before Tax	2,149	1,444	48.9	2,127	1,886	14.0
Tax	822	311	164.4	667	471	74.3
Profit After Tax	1,328	1,133	17.2	1,460	1,414	(6.1)

Source: Company, Centrum Research

- **Loan growth healthy at 27%:** The loan growth during the quarter was quite healthy at 27% YoY, though moderate in comparison to +30% as quality credit deployment opportunities thinned. From a segmental perspective, mortgages grew by a strong 57% YoY and 12% QoQ. The management expects to clock 25-27% YoY loan growth for FY2013, as the seasonal pick up in credit demand during H2FY13 starts flowing in.
- **Fx revaluation contains other income:** Non-interest income grew by muted 14% YoY during the quarter led by a change in accounting for forex transactions which resulted in a loss of Rs70mn. However, core fee income grew by a healthy 17% YoY and treasury gains rose significantly to Rs95mn.
- **Opex jumps on branch additions:** Operating expenses grew by 32% YoY during the quarter led by both staff and other expenses. The high growth in opex was primarily led by aggressive branch expansion (target of 100 additions in FY13) and increase in dearness allowance.
- **Maintain Buy:** Notwithstanding the challenges on loan growth, we draw significant comfort on KVB's strong asset quality matrix characterized by a limited restructured portfolio, strong PCR and comfortable GNPA position. The ability to deliver robust return ratios on consistent basis despite challenging environment reflects strong management quality and grasp of focus segments. At the current price, the stock trades at 6.6x FY14E EPS and 1.5x FY14E ABVPS. We maintain Buy with a revised target price of Rs550.

Y/E Mar (Rsmn)	NII	NonInt. Inc.	Adj PAT	YoY %	EPS (Rs)	P/E (x)	Adj BV (Rs)	P/Adj BV (x)	ROE (%)	ROA (%)
FY11	7,669	2,643	4,176	24.3	44.2	10.6	224.7	2.1	22.2	1.7
FY12	9,171	3,502	5,017	20.1	46.8	10.0	245.3	1.9	20.7	1.5
FY13E	12,028	4,252	6,105	21.7	57.0	8.2	267.3	1.8	21.0	1.5
FY14E	14,850	4,965	7,590	24.3	70.8	6.6	309.7	1.5	22.5	1.5
FY15E	18,295	5,718	9,778	28.8	91.2	5.1	364.6	1.3	24.6	1.6

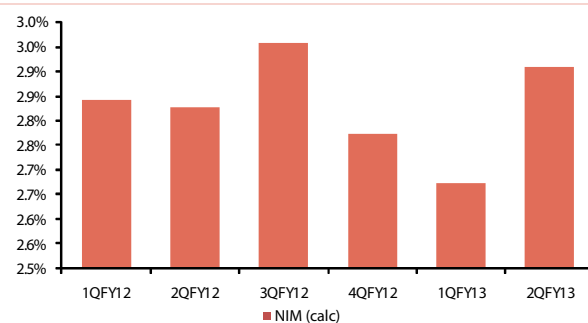
Source: Company, Centrum Research Estimates

Key Data

Target Price	Rs550	Bloomberg Code	KVB IN
CMP	Rs469*	Reuters Code	KARU.BO
Upside	17%	Current Shares O/S (mn)	107.2
Stock to Sector	Outperform	Diluted Shares O/S(mn)	107.2
Sector to Market	Outperform	Mkt Cap (Rsbn/USDbn)	50.3/923.5
Price Performance (%)*		52 Wk H / L (Rs)	482/315
	1M	6M	1Yr
KVB	10.3	16.8	18.0
NIFTY	(0.4)	12.5	8.3
	Daily Vol. (3M NSE Avg.)		92,645
	Face Value (Rs)		10
	USD = Rs54.5		

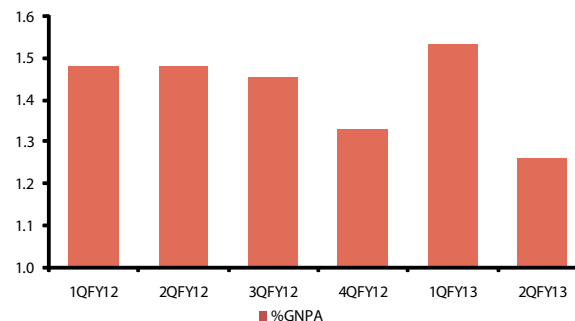
Source: Bloomberg, Centrum Research
*as on 06 November 2012

Smart improvement in NIM



Source: Company, Centrum Research

Positive surprise on GNPA (improvement of 30bps QoQ)



Source: Company, Centrum Research

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Centrum Equity Research is available on Bloomberg, Thomson Reuters and FactSet

Financials

Exhibit 1: Income Statement

Y/E March (Rsmn)	FY11	FY12	FY13E	FY14E	FY15E
Interest Income	22,177	32,704	40,998	49,364	60,039
Interest Expense	14,508	23,533	28,971	34,514	41,744
Net Interest Income	7,669	9,171	12,028	14,850	18,295
YoY Growth (%)	35.8	19.6	31.1	23.5	23.2
Non Interest Income	2,643	3,502	4,252	4,965	5,718
YoY Growth (%)	6.9	32.5	21.4	16.8	15.2
Fee & Other Income	2,266	3,124	3,752	4,415	5,118
Treasury gain	377	377	500	550	600
Total Net Income	10,312	12,673	16,280	19,815	24,013
Total Operating Expenses	4,306	5,416	6,970	8,099	9,663
YoY Growth (%)	23.5	25.8	28.7	16.2	19.3
Employee Expenses	2,295	2,644	3,513	3,996	4,768
Other Operating Expenses	2,011	2,772	3,457	4,103	4,895
PPP (Pre-excep)	6,006	7,257	9,310	11,716	14,350
Pre-provision Profit	6,006	7,257	9,310	11,716	14,350
Provisions & Contingencies	373	938	1,169	1,596	2,035
NPA Provisions	100	191	1,006	1,296	1,648
Other Provisions	273	747	164	301	387
Profit Before Tax	5,633	6,319	8,140	10,119	12,316
Taxes	1,457	1,302	2,035	2,530	2,538
Net Profit	4,176	5,017	6,105	7,590	9,778
Adj Net Profit	4,176	5,017	6,105	7,590	9,778

Source: Company, Centrum Research Estimates

Exhibit 2: Balance Sheet

Y/E March (Rsmn)	FY11	FY12	FY13E	FY14E	FY15E
Cash & balance with RBI	16,798	19,209	30,561	32,134	45,875
Inter-bank borrowings	946	1,146	1,514	1,789	2,262
Loans & Advances	178,145	239,492	298,214	374,209	441,567
Investments	77,318	105,061	126,793	161,092	192,059
Total Int Earning Assets	273,206	364,907	457,082	569,223	681,764
Fixed Assets	2,106	2,449	2,900	3,733	4,407
Other Assets	6,936	8,993	(14,262)	797	(8,732)
Total Assets	282,248	376,349	445,719	573,753	677,439
Deposits	247,218	321,116	401,395	495,723	604,782
Other Int Bearing Liab	5,296	19,726	(906)	25,786	6,030
Interest Bearing Liab	252,514	340,842	400,489	521,508	610,811
Other non int Liab	8,361	8,425	14,172	15,890	23,507
Total Liabilities	260,875	349,267	414,661	537,399	634,318
Equity	21,370	27,082	31,059	36,355	43,121
Total Liabilities	282,245	376,349	445,719	573,753	677,439

Source: Company, Centrum Research Estimates

Exhibit 3: Key Ratios

Y/E March (Rsmn)	FY11	FY12	FY13E	FY14E	FY15E
BS Structure Ratios (%)					
Loans/Deposits	72.1	74.6	74.3	75.5	73.0
Investments / Deposits	31.3	32.7	31.6	32.5	31.8
CASA Ratio	23.3	21.0	23.5	23.5	23.5
Loan Growth	32.0	34.4	24.5	25.5	18.0
Deposit Growth	28.3	29.9	25.0	23.5	22.0
Operating Ratios (%)					
NIM	3.1	2.8	2.9	2.9	2.9
Non-int income/Net income	25.6	27.6	26.1	25.1	23.8
Emp Costs (% of Opex)	53.3	48.8	50.4	49.3	49.3
Cost/Income	41.8	42.7	42.8	40.9	40.2
Operating cost growth	23.5	25.8	28.7	16.2	19.3
Total prov as % of avg. loans	0.2	0.4	0.4	0.5	0.5
Tax Rate (%)	25.9	20.6	25.0	25.0	20.6
Credit Quality Ratios (%)					
Gross NPA	1.4	1.3	1.7	1.8	1.9
Net NPA	0.4	0.3	0.8	0.8	0.9
Slippage	0.4	1.0	1.3	1.1	1.1
NPA coverage ratio	93.9	83.9	59.7	57.6	56.5
Profitability Ratios (%)					
RoAE	22.2	20.7	21.0	22.5	24.6
RoAA	1.7	1.5	1.5	1.5	1.6
Valuations Ratios					
BVPS (Rs)	226.2	252.7	289.8	339.2	402.3
Price/BV (x)	2.1	1.9	1.6	1.4	1.2
Adjusted BVPS (Rs)	224.7	245.3	267.3	309.7	364.6
Price/Adj. BV (x)	2.1	1.9	1.8	1.5	1.3
EPS (Rs)	44.2	46.8	57.0	70.8	91.2
P/E (x)	10.6	10.0	8.2	6.6	5.1
Dividend Yield (%)	2.9	3.0	3.6	3.9	5.2

Source: Company, Centrum Research Estimates

Appendix A

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