

Karur Vysya Bank Ltd – Q2FY13 result update

Asset quality shines, growth momentum continues

CMP INR: 472

Target Price INR: 570

Karur Vysya Bank (KVB) Q2FY13 operating performance was in line with our estimates, it reported PAT of INR 133 crs (up 17% YoY), marginally below our estimates mainly due to high tax rate of 38% in current quarter. Asset quality performance was commendable with no NPA increase. GNPA declined to 1.26% vs 1.53% QoQ and NNPA's declined to 0.3% vs 0.4% QoQ. No major restructuring was seen during the quarter a remarkable achievement given the higher share of SME loan book at 35%. NII grew at an impressive pace of 32% led by 27% loan book growth.

Advances growth robust, NIMs expand in Q2FY13

KVB's advances growth remained robust in Q2FY13, expanding 27% YoY and 4% QoQ to INR 25,670 crs. Although the growth was more broad-based across segments, traction was higher in commercial, retail & gold loans segments. Deposits grew by 23% YoY and 1.5% QoQ to INR 33,444 crs, led by strong growth in CASA deposits. CASA deposits improved by 2% QoQ to 22%. We are estimating an advances and deposit growth of 25% in FY13E.

NIMs (reported) improved by 24bps to 3.06% on QoQ basis, primarily due to declined in cost of deposits by ~19bps QoQ to 8.34%, while yield on advances improved by ~5bps QoQ to 12.91%, translating into NIM expansion of 24bps to 3.06%. NIMs are expected to bottom out given the correction in wholesale rates. Going forward, we expect net interest margins to remain in the range of 3.0% to 3.2% for FY13E. Net interest income grew 32% YoY to INR 285crs, led by strong advances growth of 27%.

Commendable performance on asset quality

KVB's headline asset quality performance was commendable with no NPL increase given the tough macro environment. GNPA declined to 1.26% vs 1.53% QoQ and NNPA's declined to 0.3% vs 0.4% QoQ. Lower slippages of 1% and strong recoveries/upgrades resulted in declined in GNPA's. No major restructuring was seen during the quarter a remarkable achievement given the higher share of SME loan book at 35%. Restructured assets remained comfortable at 2.7% of advances. Provisioning coverage stands comfortable at 75%. Management has re-iterated its comfort on asset quality.

Outlook and valuation: Attractive, re-iterate "Buy"

Led by strong business traction and stable asset quality, we expect KVB to register growth of 23% CAGR in PAT over FY12-14E. The stock is currently trading at 1.4x FY13E ABV, attractive for a strong regional franchise with RoE of 21% and RoA of 1.5%. We re-iterate "BUY" with a revised target price of INR 570; valuing the bank at 1.7x FY14E adjusted book value. (Upside potential of 21% + Dividend yield of 3%).

Year To Mar (INR Crs)	Q2FY13	Q2FY12	YoY (%)	Q1FY13	QoQ (%)	FY12	FY13E	FY14E
NII + OI	286	216	32.0	254	12.5	1267	1606	1893
PPOP	194	158	23.2	203	(4.9)	726	951	1111
Core PAT	133	113	17.2	146	(9.0)	501	622	762
Diluted EPS (INR)	12.4	10.6	17.2	13.6	(9.0)	46.8	58.1	71.2
Diluted P/E (x)						10.0	8.1	6.6
P/ABV (x)						2.0	1.7	1.4
ROAE (%)						20.8	21.2	22.3
Gross NPA (%)						1.3	1.5	1.3
Net NPA (%)						0.3	0.4	0.3

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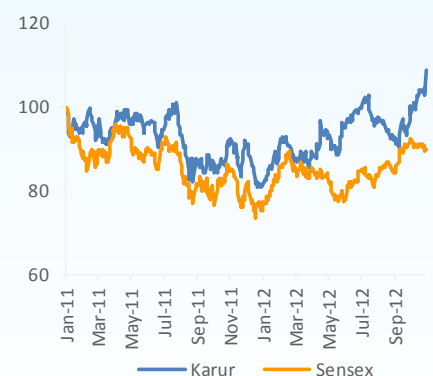
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Bloomberg:	KVB:IN
52-week range (INR):	481/ 315
Share in issue (Crs):	10.7
M cap (INR bn):	50
Avg. Daily Vol. BSE/NSE :('000):	68

Promoters:	3.23
DII's:	7.84
FII's:	22.78
Public:	66.15



Date: 1st November, 2012

Q2FY13 Result Highlights

Other highlights:

- CAR at 14%, Tier-I capital at 12.7%. The bank is well capitalized for medium-term growth.
- Cost to Income ratio inched up to 47.6% vs 43.4% QoQ mainly due to increase in operating expenses by 13%QoQ due to opening of 21 branches during the quarter.
- Opened 21 branches in Q1FY13 taking the total branch count to 475.

INR (Cr.)	Q2FY13A	Q2FY12	Growth (%)	Q1FY13	Growth (%)
Interest Income	1039	772	34.5	1006	3.3
Interest Expended	753	556	35.5	752	0.2
Net Interest Income	286	216	32.0	254	12.5
Other Income	85	75	13.8	104	-18.5
Net Total Income	371	291	27.3	358	3.5
Employee Expenses	82	60	36.4	75	10.0
Operating Expenses	94	73	28.7	81	16.6
Total Expenses	177	134	32.2	156	13.4
Pre Provision Profits	194	157	23.2	203	-4.1
Provisions & Contingencies	-21	13	-255.1	-10.0	106.5
Profit Before Tax	215	144	48.9	213	1.1
Provision for Tax	82	31	164.4	67	23.2
Adjusted Net Profit After Tax	133	113	17.2	146	-9.0
EPS (INR)	12	11	17.2	14	-9.0
No. of Shares (Cr.)	10.7	10.7		10.7	
Face Value (INR)	10.0	10.0		10	
Net Interest Margin(%) (Reported)	3.06	3.41		2.82	
Capital Adequacy Ratio (Basel II)	14	14		15	
Tier I Capital	12.7	12.8		13.5	
Asset quality					
Gross Non Performing Assets	322.7	298.2	8.2	376.9	-14.4
(%) Gross Non Performing Assets	1.26	1.48		1.53	
Net Non Performing Assets	80.2	58.2	37.7	92.3	-13.1
(%) Net Non Performing Assets	0.32	0.29		0.38	
Provision Coverage Ratio(%)	75.2	80.5		75.5	
Balance sheet (INR crore)					
Total Advances	25670	20216	27.0	24619	4.3
Total Deposits	33444	27121	23.3	32952	1.5
CASA %	22%	22%		20.4%	
Credit-Deposit Ratio	76.8	74.5		75	

Source: Company, Edelweiss research.

Business Overview:

Incorporated in 1916, KVB is a private sector bank headquartered in Tamil Nadu. It is one of the oldest banks in India and among very few banks that has remained profitable throughout its operating history. KVB is a leading bank in South India with widespread presence across Tamil Nadu, Andhra Pradesh and Karnataka. The bank's staff strength is ~5400, with 451 branches and 825 ATMs across India and all its branches are covered under Core Banking Solutions (CBS). Branches in the South region account for 81% of its network and 69% of total business.

The bank plans to increase its number of branches to 800 over the next four years. In FY13E, the bank plans to grow its advances and deposits by 25%. KVB's balance sheet size was ~INR376 bn in FY12 with market cap of INR 44 bn.

Investment Theme:

Robust business growth to continue: We expect KVB's advances to grow at a CAGR of 25% over FY12-14 (FY02-FY12 CAGR of 26%), driven by continued thrust on short-term working capital loans and gold loans.

Liability franchise to improve: High deposit growth trajectory of 25% plus likely over FY11-13E on the back of branch network expansion and product innovation.

Healthy asset quality, provision coverage in line with RBI norms, limited restructuring and strong operating efficiency.

Attractive valuations, one of the best return ratios and asset quality in the industry.

Key Risks:**Higher than expected delinquencies**

Economic downturn may result in deterioration in asset quality and adversely affect profitability of the bank. We have built in higher delinquencies for KVB in our projections. Moreover, higher than expected slippages on restructured assets can risk asset quality.

Slowdown in economy

Future profitability and revenue growth of Indian banks depends on the country's macroeconomic factors. Hence, any slowdown in growth rate of the Indian economy or any major change in economic factors may alter our recommendations.

Financials

Income Statement (INR Cr)	FY10	FY11	FY12	FY13E	FY14E
Interest Income	1758	2218	3270	3950	4650
Interest Expenses	1193	1451	2353	2729	3181
Net Interest Income	565	767	917	1221	1469
Other Income	247	264	350	385	424
Net Total Income	812	1031	1267	1606	1893
Provision for Employees	163	230	264	317	381
Operating Expenses	85	107	134	166	206
Depreciation	23	30	38	46	51
Other Expenses	78	64	105	125	144
Total expenses	349	431	542	655	782
Pre Provision Profits	463	601	726	951	1111
Provisions and Contingencies	37	39	94	131	108
Net Profit Before Tax	426	561	631	819	1003
Provision for Tax	90	146	130	197	241
Fringe Benefit Tax	0	0	0	0	0
Net Profit After Tax	336	415	501	622	762
EPS (INR)	31.5	38.8	46.8	58.1	71.2
Operating Ratio's (%)	FY10	FY11	FY12	FY13E	FY14E
Other Income /Total Income	12.3	10.6	9.7	8.9	8.4
Interest Expen / Interest Earned	67.9	65.4	72.0	69.1	68.4
Yield on Funds	9.0	8.8	9.9	9.3	8.9
Yield on Advances	11.2	10.8	12.2	11.5	10.8
Yield on Investments	7.0	7.3	7.9	7.2	7.2
Cost of Funds	6.1	5.8	7.1	6.4	6.1
Cost of Deposits	6.8	6.4	8.1	7.5	7.0
Interest Spread	2.5	2.7	2.3	2.6	2.6
Net Interest Margins (Calc)	3.17	3.35	3.05	3.16	3.08
Return on Average Equity	22.6	22.2	20.8	21.2	22.3
Return on Assets	1.7	1.7	1.5	1.5	1.5
Cost to Income	42.9	41.8	42.7	40.8	41.3
Operating Expen / Assets	1.6	1.5	1.4	1.4	1.4
Tax Rate (%)	21	26	21	24	24
Growth Metrics (%)	FY10	FY11	FY12	FY13E	FY14E
Net Interest Income	37.6	35.8	19.6	33.1	20.4
Total Expenses	35.3	23.5	25.8	21.0	19.4
Pre Provision Profits	10.7	29.7	20.8	31.0	16.9
Provisions and Contingencies	-57.2	5.2	140.1	39.3	0.0
Net Profit After Tax	42.4	23.7	20.7	24.2	22.5

Balance Sheet (INR Cr)	FY10	FY11	FY12	FY13E	FY14E
Sources of Funds					
Share Capital	54	94	107	107	107
Total Reserves	1566	2020	2601	3049	3588
Networth	1620	2115	2708	3156	3695
Deposits	19272	24722	32112	40139	50174
Borrowings	476	530	1973	2663	2530
Other Liabilities & Provisions	575	868	853	1099	1246
Total Liabilities	21943	28235	37646	47057	57645
Application of Funds					
Cash & Balances with RBI	1198	1680	1921	2588	2882
Balances with Banks & money at Call	37	95	115	126	126
Net Investments	6602	7732	10506	12705	14988
Advances	13447	17814	23949	29936	37421
Fixed Assets	138	211	245	294	323
Other Assets	521	703	910	1407	1905
Total Assets	21943	28235	37646	47057	57645
Balance Sheet Ratio	FY10	FY11	FY12	FY13E	FY14E
Credit-Deposit (%)	69.8	72.1	74.6	74.6	74.6
Credit Growth (%)	29.2	32.5	34.4	25.0	25.0
Deposit Growth (%)	27.6	28.3	29.9	25.0	25.0
Gross NPA (%)	1.8	1.3	1.3	1.5	1.3
Net NPA (%)	0.2	0.1	0.3	0.4	0.3
Provision Coverage (%)	86.9	93.9	75.5	72.8	77.6
CASA Ratio (%)	23.5	23.3	19.2	19.9	19.9
Capital Adequacy (%) (Basel 2)	14.5	14.4	14.3	12.7	11.8
Valuation Metrics	FY10	FY11	FY12	FY13E	FY14E
Price To Earnings (P/E)	14.9	12.1	10.0	8.1	6.6
Diluted EPS (INR)	31.5	38.8	46.8	58.1	71.2
EPS Growth (%)	42.4	23.1	20.7	24.2	22.5
No. of Shares in Crs	10.7	10.7	10.7	10.7	10.7
DPS (INR)	12.0	12.0	14.0	13.9	17.8
Dividend Payout (%)	38.1	31.0	29.9	24.0	25.0
Dividend Yield (%)	2.6	2.6	3.0	3.0	3.8
Book Value (INR)	151.9	197.4	252.9	294.7	345.0
Price to Book Value	3.1	2.4	1.9	1.6	1.4
Adjusted Book Value (INR)	143.9	187.3	235.5	273.5	335.0
Price to Adjusted Book Value	3.3	2.5	2.0	1.7	1.4

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