



## Karnataka Bank Q3 FY16 Quarterly Update

### MARKET DATA

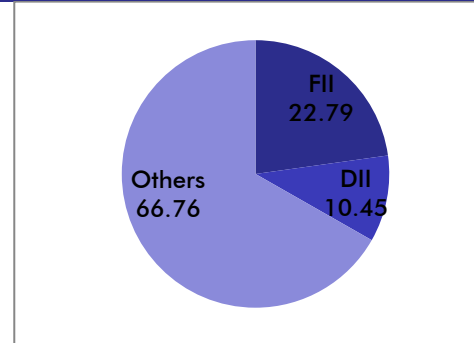
Fig. in ₹ (in Cr.) except Ratios

Networth (FY16E) (Rs. Crs)	3,673
P/BV Ratio (FY16E) (x)	0.5
EPS (FY16E) (Rs.)	21
Market Price	100
P/E Ratio (FY16E) (x)	4.6
52 Week High (7/7/2015)	158
52 Week Low (18/1/2016)	94
Market Capitalisation (Rs. crs)	1,825

### AVERAGE MONTHLY VOLUME ('000)

BSE	218.7
NSE	1,888.7

### SHARE HOLDING PATTERN



RETURN	3M	6M	12M
Stock	-23%	-30%	-36%
BSE	-12%	-15%	-17%

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For Q3FY16, Karnataka bank reported PAT of Rs 97 crs (down 5% q-o-q & 9% y-o-y) mainly because of increase in provisions (up 80% q-o-q & down 20% y-o-y). Gross NPA increased by 38bps q-o-q (12bps y-o-y) to 3.56% in Q3 FY16. NII increased to Rs. 305crs. in Q3 FY16, while POPP growth was 13% q-o-q (5% y-o-y) at Rs.192 crs.

### Asset quality deteriorated

Slippages increased by 155% q-o-q (34% y-o-y) to Rs. 380 crs; largely contributed by 6 accounts (Rs. 240 crs, in services & corporate segment). Management highlighted that Rs.150 crs. are written off in the books of branches but not at the head-office and expect them to correct in the coming quarters. GNPA increased by 38bps q-o-q (12bps y-o-y) to 3.56%. GNPA in absolute terms increased by 14% q-o-q (13% y-o-y) to Rs. 1,187 crs. NNPA fell by 45bps q-o-q (0bps y-o-y) to 2.41%. Restructured book stood at Rs. 2,335 crs. There was one SDR case (steel account) and no 5:25 refinancing during the quarter. Management guided to contain the GNPA's below 3% by FY16. Security receipts are Rs. 285 crs.

### Loan book growth flattish; however the focus is on retail book

Loan book growth remained flattish at 2% q-o-q (up 9% y-o-y) to Rs. 32,928 crs. The bank is increasing its focus on the retail book. The retail mix as % of total loan book has improved (52% in Q3FY16 vs 49% in Q3FY15). Within retail, growth was driven by MSME (up 49%), Housing (up 19%) and Personal loans (up 31%). Management guided for an above-average industry loan growth in FY16, with continued focus on the retail segment.

### NIMs remained steady; Improvement in Opex & CASA

NIMs declined by 7bps q-o-q (4bps y-o-y) to 2.34%. Yield on advances declined by 21bps q-o-q (42bps y-o-y) to 11.6%. The cost of deposit declined 6bps q-o-q (29bps y-o-y) to 7.61%. Opex to loan book stood at 2.99% (down 20bps q-o-q & 73bps y-o-y). CASA improved by 96bps q-o-q (126bps y-o-y) to 25.22%.

### Outlook & Valuation

While the credit growth for the current year has been anaemic, we expect credit growth to pick up in FY17 driven by improving Indian GDP. According to management, most of the stress has been accounted for and they foresee less slippages doing forward. We maintain a BUY rating with a target price Rs.135 (1.2x FY17E Adj.BV of Rs.112 after providing for 70% provisioning shortfall on GNPA & Security Receipts and 50% on restructured assets).

### Quarterly Performance:

Particulars (Rs in crs)	Q3 FY16	Q3 FY15	% YoY	Q2 FY16	%QoQ	FY15	FY14	% YoY
Interest Income	1,237	1,202	3%	1,248	-1%	4,698	4,189	12%
Interest Expenses	932	900	4%	941	-1%	3,530	3,133	13%
Net Interest Income	305	302	1%	307	-1%	1,169	1,056	11%
Other Income	133	163	-18%	121	10%	507	505	0%
Total Income	438	465	-6%	428	2%	1,676	1,561	7%
Operating Expenses	246	282	-13%	258	-5%	953	875	9%
Operating Profits before provisions	192	183	5%	169	13%	723	687	5%
Total Provisions	63	79	-20%	35	80%	214	278	(23)%
PBT	129	104	23%	134	-4%	542	408	33%
Taxes	32	(3)	-1332%	32	-1%	91	98	(7)%
PAT	97	107	-9.4%	102	-5%	451	311	45%

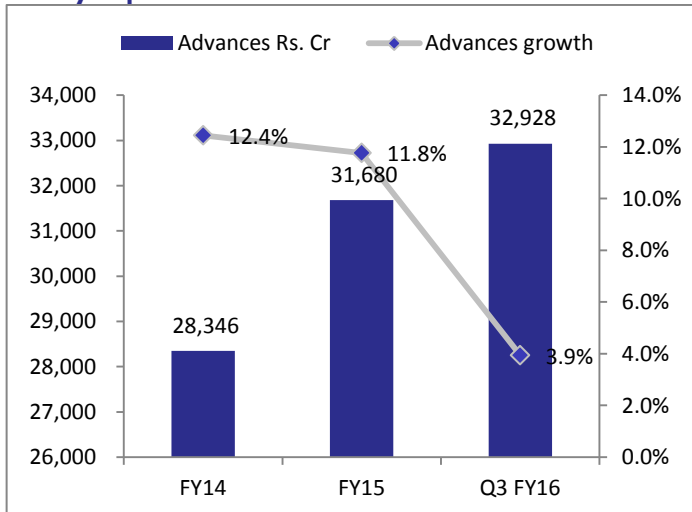


## Q3 FY16 CONFERENCE CALL HIGHLIGHTS: -

- Management does not expect any major accounts under the watch list (apart from couple of accounts totalling Rs. 50-60 crs)
- Bank has not received any communication from RBI regarding the corporate list.
- Sale to ARCs was Rs.154 crs, of this net book value (excluding provisions) of Rs.76 crs and bank sold it for Rs. 56 crs. The loss will be amortised over next 8 quarters.
- For Q3 FY16, Slippages from restructured book were Rs. 17 crs (3 accounts). Management expect one account of Rs.40-50 crs (thermal power sector) to slip into NPAs in the coming quarter.
- Security Receipts stood at Rs. 285crs.
- Management plans to increase the CASA ratio from 25.2% to 27% by FY20.
- Management is still evaluating the impact of MCLR regime and will be applicable from 1<sup>st</sup> April 2016.
- RIDF – Rs.1627crs

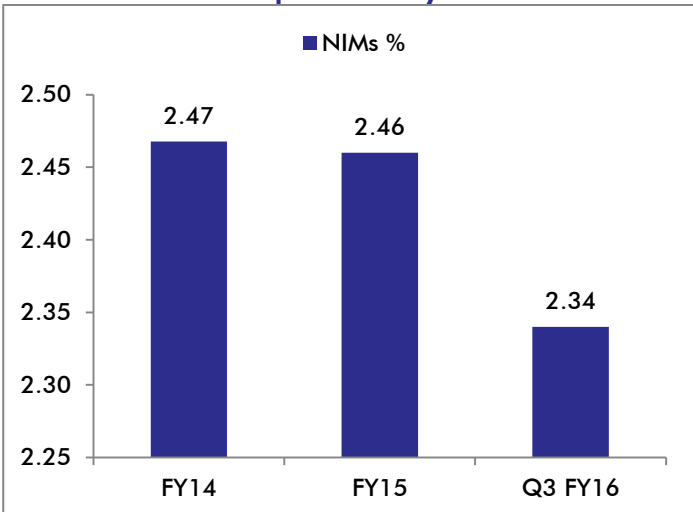
### Graphs for important parameters

#### Steady improvement in loan book

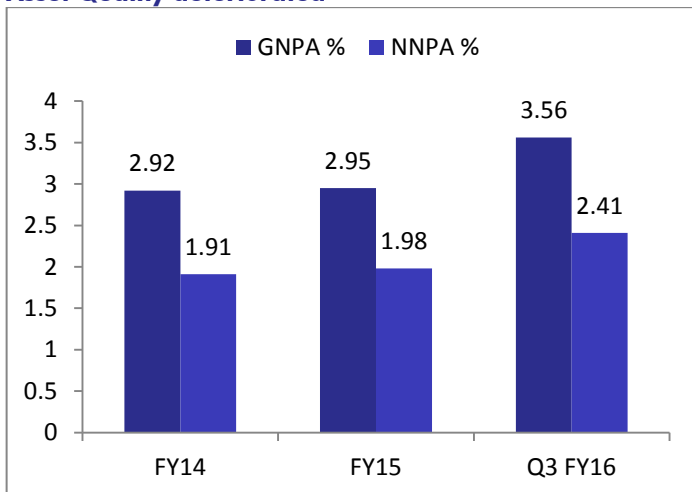


Source: Company, Dimensional Securities

#### NIMs declined due to pressure on yields

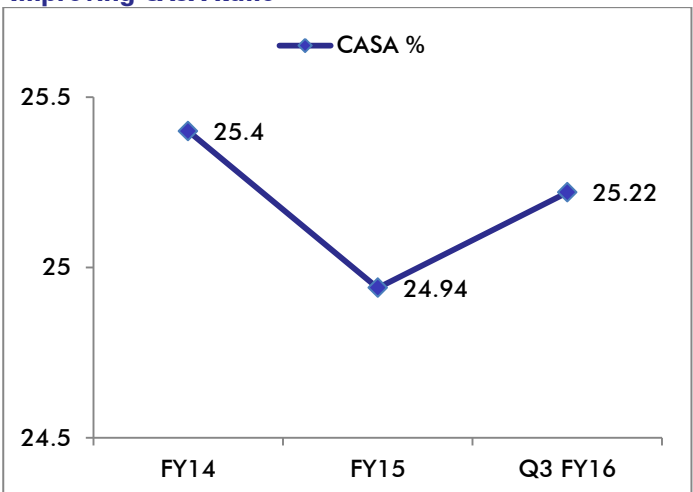


#### Asset Quality deteriorated



Source: Company, Dimensional Securities

#### Improving CASA Ratio





**QUARTERLY PERFORMANCE:**

Particulars (Rs in crs)	Dec-15	Dec-14	y-o-y	Sep-15	q-o-q	FY15	FY14	y-o-y
Interest Income	1,237	1,202	3%	1,248	-1%	4,698	4,189	12%
Interest Expenses	932	900	4%	941	-1%	3,530	3,133	13%
Net Interest Income	305	302	1%	307	-1%	1,169	1,056	11%
Other Income	133	163	-18%	121	10%	507	505	0%
Fee & Forex Income	113	132	-14%	108	5%	394	404	-2%
Total Income	438	465	-6%	428	2%	1,676	1,561	7%
Operating Expenses	246	282	-13%	258	-5%	953	875	9%
Employee	112	188	-40%	125	-10%	525	525	0%
Others	134	94	42%	134	0%	428	349	23%
Operating Profits before provisions	192	183	5%	169	13%	723	687	5%
Total Provisions	63	79	-20%	35	80%	214	278	-23%
PBT	129	104	23%	134	-4%	542	408	33%
Taxes	32	(3)	-1332%	32	-1%	91	98	-7%
PAT	97	107	-9.4%	102	-5%	451	311	45%
EPS	5.2	5.7	-9%	5.4	-5%	24.0	16.5	45%
<b>Asset Quality</b>								
GNPA Rs. Cr	1,186.6	1,054	13%	1,044	14%	944	836	13%
NNPA Rs. Cr	791	727	9%	635	24%	624	538	16%
GNPA %	3.56	3.44	12	3.18	38	2.95	2.90	5
NNPA %	2.41	2.4	0	1.96	45	1.98	1.9	8
PCR % Calculated	33.37	31.03	234	39.13	-576	33.96	35.64	-168
PCR % Reported	0	0	0	0	0	50.54	53.21	-267
Slippages	380	283	34%	149	155%	930	654	42.18%
Slippage Ratio %	1.15	0.93	22	0.46	69	2.94	2.31	63
Restructured Assets	2,335	1,978	18%	2,195	6%	2,024	1,861	9%
Credit Cost %	0.77	1.04	-27	0.43	33	0.68	0.98	-31
<b>Ratios %</b>								
Fees to Advances	1.37	1.74	-37	1.33	4	1.24	1.43	-18
Cost to Income ratio	56.20	60.58	-438	60.40	-419	56.84	56.02	82
Tax Rate	24.62	-2.46	2709	23.92	71	16.76	23.90	-714
Loan/Deposit	66.33	67.72	-139	66.38	-6	68.86	69.85	-99
CASA %	25.22	23.96	126	24.26	96	24.94	25.4	-46
RoA %	0.7	0.85	-15	0.8	-10	0.91	0.71	20
RoE %	11.61	13.18	-157	12.11	-50	14.02	10.53	349
CAR (Basel III) %	11.67	11.79	-12	11.7	-3	12.41	13.2	-79
Tier I %	10	9.84	16	10.05	-5	10.52	10.73	-21
Tier II %	1.67	1.95	-28	1.65	2	1.89	2.47	-58
Opex to Loan book	2.99	3.71	-73	3.19	-20	3.01	3.09	-8
<b>Margins %</b>								
Yield on Advances	11.64	12.06	-42	11.85	-21	11.97	12.17	-20
Cost of Deposits	7.61	7.9	-29	7.67	-6	7.87	7.9	-3
Quarterly NIMs	2.34	2.38	-4	2.41	-7	2.36	2.4	-4
BV-Calculated	197	179	10.0%	191	2.9%	180	162	11.00%
Adj. BV*	155	140	10.2%	157	-1.8%	147	133	9.96%
<b>Balance sheet</b>								
Capital	188	189	0%	188	0%	188	188	0%
Net Worth	3,697	3,369	9.7%	3,601	2.7%	3,389	3,052	11.04%
Deposits	49,644	44,799	10.9%	48,872	1.6%	46,009	40,583	13.37%
Investments	16,561	16,900	-2.0%	16,395	1.0%	15,988	15,227	5.00%
Loans	32,928	30,338	8.5%	32,443	1.5%	31,680	28,346	11.76%

\*Adj. BV= BV – NNPA

Source – Company, Dimensional Securities

**ROA TREE:**

Particulars	Dec-14	Mar-15	Jun-15	Sep-15	Dec-15	FY15	FY14
Interest Income	10.0%	9.7%	9.7%	9.5%	9.3%	9.5%	9.5%
Interest Expenses	7.5%	7.3%	7.1%	7.2%	7.0%	7.1%	7.1%
Net Interest Income	2.5%	2.4%	2.6%	2.3%	2.3%	2.4%	2.4%
Other Income	1.4%	0.9%	0.9%	0.9%	1.0%	1.0%	1.1%
Total Income	3.9%	3.3%	3.6%	3.3%	3.3%	3.4%	3.5%
Operating Expenses	2.4%	1.7%	1.7%	2.0%	1.9%	1.9%	2.0%
Employee	1.6%	0.7%	0.8%	1.0%	0.8%	1.1%	1.2%
Others	0.8%	1.1%	0.9%	1.0%	1.0%	0.9%	0.8%
Operating Profits before provisions	1.5%	1.5%	1.9%	1.3%	1.4%	1.5%	1.6%
Total Provisions	0.7%	0.0%	0.9%	0.3%	0.5%	0.4%	0.6%
PBT	0.9%	1.6%	1.0%	1.0%	1.0%	1.1%	0.9%
Taxes	0.0%	0.5%	0.1%	0.2%	0.2%	0.2%	0.2%
PAT (RoA)	0.9%	1.1%	0.9%	0.8%	0.7%	0.9%	0.7%
Average Assets/ Average Equity	14.83	15.35	15.22	15.30	15.03	15.35	14.99
RoE	13.3%	16.7%	13.2%	11.9%	11.0%	14.0%	10.5%

Source: Company, Dimensional Securities



## OUTLOOK & VALUATION: -

Karnataka bank has a strong regional presence and good technology network. The bank has well capitalized Tier 1 position at ~10% and healthy loan book of 51% in retail.

We expect loan book to grow at 11% CAGR (FY15-18E). Backed by operating performance, we expect RoA and RoE to be 0.8% and 12% by FY18E respectively.

While the credit growth for the current year has been anaemic, we expect credit growth to pick up in FY17 driven by improving Indian GDP. According to management, most of the stress has been accounted for and they foresee less slippages doing forward. We maintain a BUY rating with a target price Rs.135 (1.2x FY17E Adj.BV of Rs.112 after providing for 70% provisioning shortfall on GNPA & Security Receipts and 50% on restructured assets).

### P/BV (Forward)



Source: Dimensional Securities

**PROFIT & LOSS STATEMENT:**

Particulars, Rs Cr	FY14	FY15	FY16E	FY17E	FY18E
Interest Earned	4,189	4,698	4,909	5,272	5,854
Interest expended	3,133	3,530	3,652	3,928	4,300
Net Interest Income	1,056	1,169	1,257	1,345	1,554
Other Income	506	507	487	540	651
NII+ Other Inc.	1,562	1,676	1,743	1,885	2,205
Employees Cost	525	525	451	483	554
Op, Admin & Other expenses	349	392	508	544	625
Profit Before Provision & Contingencies	687	759	784	858	1,025
Provisions & Contingencies	278	214	283	279	278
PBT	409	545	502	578	747
Provision for Tax	98	91	110	173	254
PAT	311	454	391	405	493

Source: Company, Dimensional Securities

**BALANCE SHEET STATEMENT:**

Particulars, Rs. Cr	FY14	FY15	FY16E	FY17E	FY18E
<b>SOURCES OF FUNDS :</b>					
Capital	188	188	188	188	188
Reserves	2,861	3,201	3,482	3,776	4,148
Total Shareholders' Funds	3,049	3,389	3,670	3,965	4,336
Deposits	40,583	46,009	50,149	55,164	60,681
Borrowings	1,915	1,038	1,164	1,304	1,500
Other Liabilities	1,479	1,401	1,684	1,963	2,242
<b>TOTAL LIABILITIES</b>	<b>47,026</b>	<b>51,837</b>	<b>56,668</b>	<b>62,396</b>	<b>68,759</b>
<b>APPLICATION OF FUNDS :</b>					
Cash & Bank Balances	2,337	2,614	4,775	4,991	4,679
Investments	15,227	15,988	17,267	18,648	19,581
Advances	28,346	31,680	33,264	37,256	42,844
Fixed Assets	198	292	272	300	331
Other Assets	922	1,263	1,089	1,201	1,324
<b>TOTAL ASSETS</b>	<b>47,029</b>	<b>51,837</b>	<b>56,668</b>	<b>62,396</b>	<b>68,759</b>

Source: Company, Dimensional Securities



## RATIOS:

Particulars	FY14	FY15	FY16E	FY17E	FY18E
<b>Spread Analysis</b>					
Yield on Earning Assets	9.8%	9.9%	9.4%	9.2%	9.3%
Cost of Funds	7.6%	7.6%	7.2%	7.1%	7.0%
Interest Spread	2.2%	2.3%	2.2%	2.2%	2.3%
Net Interest Margin	2.5%	2.5%	2.4%	2.3%	2.5%
<b>Profitability Ratio</b>					
RoE, %	10.6%	14.1%	11.1%	10.6%	11.9%
RoA, %	0.7%	0.9%	0.7%	0.7%	0.8%
Interest Expense/Interest Income	74.8%	75.1%	74.4%	74.5%	73.5%
Non-Interest Income/Total Income	32.4%	30.3%	27.9%	28.7%	29.5%
<b>Efficiency Ratio</b>					
Cost/Income	56.0%	54.7%	55.0%	54.5%	53.5%
Employee Cost/Operating Expenses	60.1%	57.2%	47.0%	47.0%	47.0%
<b>Asset Liability Ratio</b>					
Credit/Deposit	69.8%	68.9%	66.3%	67.5%	70.6%
CASA/Deposit	25.4%	25.3%	25.2%	25.9%	26.3%
Investment/Deposits	37.5%	34.8%	34.4%	33.8%	32.3%
<b>Asset Quality</b>					
GNPA (%)	2.9%	2.9%	3.5%	3.3%	3.1%
NNPA (%)	1.9%	2.0%	2.5%	2.3%	2.1%
<b>Valuation Ratio</b>					
Book Value, Rs.	161.8	179.8	194.7	210.4	230.1
Book Value (Adjusted), Rs.	141.6	157.6	171.2	186.5	205.7
EPS, Rs.	16.5	24.1	20.8	21.5	26.2
Dividend, Rs.	4.0	5.0	5.0	5.0	5.5
P/BV, x	0.7	0.7	0.5	0.5	0.4
P/E, x	7	5	5	5	4

Source: Company, Dimensional Securities



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